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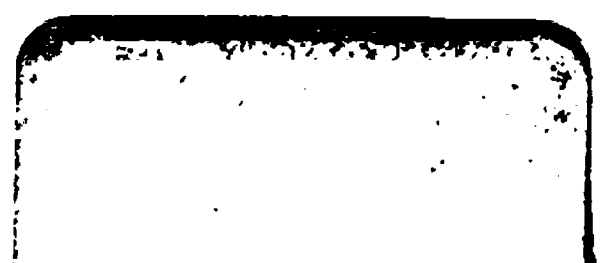
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HANDBOOK

OF THE LAW OF

PRIVATE CORPORATIONS

By WM. L. CLARK, Jr.

INSTRUCTOR IN LAW IN THE CATHOLIC UNIVERSITY OF AMERICA,
AND AUTHOR OF HORNBOOKS ON "CRIMINAL LAW," "CRIMINAL PROCEDURE,"
AND "CONTRACTS"

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To

FRANK P. CLARK, Esq.,

of Baltimore,

As a slight mark of the author's regard and of his remembrance
and sincere appreciation of many kindnesses,

THIS VOLUME IS AFFECTIONATELY DEDICATED.

(11)•

PREFACE.

There are few subjects in the law in which so many difficulties, and so great a conflict in the decisions, are to be met with as in the law of private corporations. The law is unsettled on many points. These points have received special attention in this treatise, and to some of them more space has been devoted than is given them in the larger works. For examples, reference may be made to the chapters in which are discussed the doctrines in regard to corporations de facto (page 86), estoppel to deny corporate existence (page 99), subscriptions to stock prior to incorporation (page 263), and watered stock (page 368). The doctrine, often laid down in the cases, and stated in all the text books, but which has been virtually exploded by recent decisions, that the capital stock and assets of a corporation constitute a trust fund for the benefit of creditors, has been given considerable space (page 539).

The entire work has been written from the cases themselves, and throughout his work the author has aimed at making the book a true reflection of the cases. The authorities have been selected with care, and none have been cited without personal examination.

The work is not intended to deal with corporation law in its application to particular corporations, but only with the rules and principles of law applicable to corporations generally. It would be impossible to go further than this, and keep within the limits of a handbook in one volume.

The very interesting monograph on "The Logical Conception of a Corporation," by Mr. Benjamin Trapnell, with the accompanying chart, has, with the author's permission, been inserted as an appendix, and materially adds to the value of the work.

WM. L. C., Jr.

Washington, D. C., February 6, 1897.

TABLE OF CONTENTS.

CHAPTER I.

OF THE NATURE OF A CORPORATION.

Section	Page
1-3. Corporation Defined.....	1-11
4. Creation of Corporations.....	11-12
5. Limited Powers of Corporations.....	12
6-8. Attributes and Incidents of a Corporation.....	12-23
9. Corporation as a "Person," "Citizen," etc.....	24-25
10-11. Kinds of Corporations.....	26-32

CHAPTER II.

CREATION AND CITIZENSHIP OF CORPORATIONS.

12. Creation—In General	33
13-18. Power to Create.....	33-41
14. State Legislatures	34
15. Congress	34
16. Territorial Legislatures	34
17. Prescription	34
18. Delegation of Power.....	34-41
19-20. General and Special Laws.....	42-48
21. Ratification of Claim to Corporate Existence.....	48-49
22. Intention to Create.....	49-50
23-24. Agreement between Corporation and State—Acceptance of Charter	50-54
25. Place of Organization.....	54-55
26. Compliance with Conditions Precedent.....	55-63
27. Agreement between Corporators and Corporation.....	64
28-29. Who may Become Corporators.....	64-67
30-31. Purpose of Incorporation.....	67-71
32-35. Corporate Name	71-74
36-38. Residence and Citizenship of Corporations.....	74-80
39. Extension of Charter—Creation of New Corporation.....	81-82
40. Proof of Corporate Existence.....	82-85

CHAPTER III.**EFFECT OF IRREGULAR INCORPORATION.**

Section	Page
41-42. Corporations De Facto.....	86-98
43-44. Estoppel to Deny Corporate Existence.....	99-108
45. Liability of Associates as Partners.....	108-110

CHAPTER IV.**RELATION BETWEEN CORPORATION AND ITS PROMOTERS.**

46. Liability of Corporation for Expenses and Services of Promoters	111-112
47. Liability on Contracts by Promoters.....	112-117
48. Liability of Promoters to Corporation and Stockholders.....	117-119

CHAPTER V.**POWERS AND LIABILITIES OF CORPORATIONS.**

49. In General	120-122
50. Express Powers	122
51. Powers Incidental to Corporate Existence.....	122-124
52. Powers Implied from Powers Expressly Granted.....	124
53. Construction of Charter—In General.....	124-128
54. Power to Take and Hold Real and Personal Property.....	128-132
55. Power to Act as Trustee.....	132-133
56-57. Powers as to Contracts and Conveyances.....	133-156
58-61. Form and Mode of Corporate Contracts.....	156-162

CHAPTER VI.**POWERS AND LIABILITIES OF CORPORATIONS (Continued).**

62. Effect of Ultra Vires Act—In General.....	163-164
63. A Corporation May Exceed Its Powers.....	164-166
64. Assent of Shareholders.....	166-167
65-66. Ultra Vires Conveyances of Land, or Transfers of Personality	167-170
67. Ultra Vires Contracts.....	170-187
68. Illegal Contracts	187-192

CHAPTER VII.**POWERS AND LIABILITIES OF CORPORATIONS (Continued).**

Section	Page
69. Liability for Torts.....	193-197
70-72. Responsibility for Crime—Contempt of Court.....	197-200

CHAPTER VIII.**THE CORPORATION AND THE STATE.**

73-74. Power of the State over Corporations—Charter as a Contract...	201-207
75. Police Power of the State.....	207-211
76. Power of Eminent Domain.....	211-212
77. Reservation of Power to Repeal or Amend Charter.....	212-219
78. Offer of Amendment—Power of Majority.....	219
79-81. Taxation of Corporations.....	219-230

CHAPTER IX.**DISSOLUTION OF CORPORATIONS.**

82. How Dissolution is Effected.....	231-244
83-84. Equity Jurisdiction	245-248
85. Effect of Dissolution.....	248-252

CHAPTER X.**MEMBERSHIP IN CORPORATIONS.**

86. How Membership is Acquired.....	253-255
87-88. "Capital Stock" and "Capital.".....	256-257
89-90. Nature of Shares of Stock.....	257-260
91. Certificates of Stock.....	260-261
92. Subscriptions to Stock—Subscriptions after Incorporation.....	261-263
93-97. Subscriptions Prior to Incorporation.....	263-274
98. Who may Become Subscribers.....	275-277
99. Form of Subscription—Statutory Formalities.....	277-281
100. Mutual Consent	281-283
101. Subscriptions Induced by Fraud.....	283-290
102. Subscriptions under Mistake.....	290-291
103. Subscription by Agent.....	291-292

Section		Page
104-106.	Agents to Receive Subscriptions.....	298-294
107-109.	Conditional Subscriptions	294-301
110-112.	Subscriptions upon Special Terms.....	302-306
113.	Conditional Delivery of Subscription.....	306-308
114-115.	Subscription of Entire Capital, and Distribution.....	308-313
116.	Payment of Deposit.....	313-316
117.	Delivery of Certificate.....	316-317
118-121.	Remedy of Corporation on Subscriptions.....	318-322
122-125.	Calls	322-327
126.	Assignment of Unpaid Subscription.....	328
127-132.	Release and Discharge of Subscriber.....	328-334
133.	Estoppel of Subscriber.....	335

CHAPTER XI.

MEMBERSHIP IN CORPORATIONS (Continued).

134.	Right of Members to Inspect Books and Papers of Corporation..	336-339
135.	Right to Vote at Meetings.....	340
136-137.	Profits and Dividends.....	340-358
138-140.	Increase of Capital Stock.....	358-360
141.	Shareholders' Right to Preference.....	360-361
142-145.	Preferred Stock	361-368
146-148.	Watered and Bonus Stock.....	368-389
149-151.	Action by Stockholders for Injuries to Corporation—Interference in Management.....	389-401
152.	Expulsion of Members.....	401-405

CHAPTER XII.

MEMBERSHIP IN CORPORATIONS (Continued).

153-154.	Transfer of Shares.....	406-409
155.	Effect of Transfer.....	409-413
156.	Lien of Corporation on Shares.....	413-414
157-158.	Validity of Transfers.....	415-416
159-160.	Mode of Transfer.....	416-417
161-162.	Registration of Transfer.....	417-427
163-166.	Forged and Unauthorized Transfers.....	427-434
167.	Liability of Indorser of Forged Certificate.....	434
168-169.	Liability of Corporation Arising from Unauthorized or Invalid Transfer	435-436

TABLE OF CONTENTS.

xi

Section	Page
170-171. Liability of Corporation on Certificates Issued Fraudulently, without Authority, etc.....	437-440
172. Remedy against Corporation for Refusal to Recognize Transfer..	440-441
173. Compelling Corporation to Issue New Certificates.....	441-442

CHAPTER XIII.

MANAGEMENT OF CORPORATIONS—OFFICERS AND AGENTS.

174-177. Powers of the Majority of Stockholders.....	443-453
178-181. By-Laws	454-462
182-184. Stockholders' Meetings.....	462-472
185-188. Voting	473-482
189-190. Election and Appointment of Officers and Agents.....	482-483
191. Qualifications of Directors or Other Officers.....	484-485
192. Powers of Directors.....	485-488
193-194. Directors' Meetings and Resolutions.....	488-493
195-197. Authority of Other Officers and Agents.....	493-502
198. Notice to Officer as Notice to Corporation.....	502-504
199. Contracts between Stockholder and the Corporation.....	504
200. Relation between Officers and Corporation.....	504-507
201-202. Contracts or Other Transactions between Officers and the Cor- poration	508-514
203. Liability of Officers to the Corporation.....	514-518
204-205. Remedies against Officers.....	519-520
206. Liability of Officers and Agents on Contracts.....	521-522
207-209. Liability of Corporation for Torts of Officers and Agents.....	523-530
210. Liability of Officers and Agents to Third Persons for Torts.....	530-531
211. Compensation of Officers.....	531-533
212. Removal of Officers and Agents.....	533-534
213. Relation between Officers and Stockholders.....	534-536

CHAPTER XIV.

RIGHTS AND REMEDIES OF CREDITORS.

214. Relation between Creditors and the Corporation—Remedies in General	537-538
215. Property Subject to Execution.....	538-539
216. Assets of a Corporation as a "Trust Fund" for Creditors..	539-546
217. Interference in Management of Corporation.....	546-548
218. Fraudulent Conveyances and Transfers.....	549-552
219. Suits for Injunction and Receiver.....	552-553

Section		Page
220.	Assignment for Benefit of Creditors—Preferences.....	553-554
221.	Dissolution of Corporation.....	555-556
222.	Consolidation of Corporations.....	556
223.	Extension of Charter—New Corporation.....	556-557
224.	Set-Off by Debtor of Corporation.....	557-558
225-226.	Relation between Creditors and Stockholders.....	558-564
227-230.	Statutory Liability of Stockholders.....	564-575
231.	Who are Liable as Stockholders under the Statutes.....	576-587
232-233.	Who may Enforce Statutory Liability.....	588-589
234-236.	Remedies of Creditors against Stockholders.....	589-597
237.	Necessity for Judgment against Corporation.....	597-598
238.	Effect of Judgment against Corporation.....	599-600
239.	Statute of Limitations.....	600-602
240.	Set-Off by Stockholders.....	602-604
241.	Contribution among Stockholders.....	604-605
242-243.	Relation between Creditors and Officers.....	605-608
244.	Preferences to Officers Who are Creditors.....	608-609
245.	Statutory Liability of Officers.....	609-611

CHAPTER XV.

FOREIGN CORPORATIONS.

246.	Foreign Corporations Defined.....	612
247-249.	Status of a Foreign Corporation.....	612-633
250-254.	Actions by and against.....	633-639
255.	Visitorial Power over Foreign Corporation.....	639-641

APPENDIX:

THE LOGICAL CONCEPTION OF A CORPORATION.

(Page 643.)

↑

HANDBOOK

OF THE

LAW OF PRIVATE CORPORATIONS.

CHAPTER I.

OF THE NATURE OF A CORPORATION.

- 1-3. Corporation Defined.
- 4. Creation of Corporations.
- 5. Limited Powers of Corporations.
- 6-8. Attributes and Incidents of a Corporation.
- 9. Corporation as a "Person," "Citizen," etc.
- 10-11. Kinds of Corporations.

CORPORATION DEFINED.

1. **A corporation aggregate is a collection of individuals united, by authority of law, into one body, under a special denomination, with the capacity of perpetual succession, and of acting in many respects as an individual.¹ Every corporation aggregate consists of:**
 - (a) **A collection of individuals.**
 - (b) **A legal entity, which is, for many purposes, in contemplation of law, separate and distinct from the members who compose it.***

¹ "Bodies politic and corporate have been known to exist as far back, at least, as the time of Cicero; and Gaius traces them even to the laws of Solon, of Athens, who lived some 500 years before. Poth. Panel of Just. (Paris Ed., 1828) bk. 3, p. 109. These associated bodies, or communities of individuals, with cer-

* See Appendix, post, p. 642, "The Logical Conception of a Corporation," by Benjamin Trapnell, Esq.

2. For the purpose of acquiring, holding, and conveying property, contracting obligations, incurring liabilities, suing and being sued, a corporation is regarded in law as a legal entity, separate and distinct from the members who compose it. For instance:

- (a) The property of a corporation is owned by the corporation, and not by the individual members.**
- (b) Conveyances of such property must be made by the corporation, and cannot be made by the members as individuals.**
- (c) Suits on causes of action accruing in favor of or against a corporation must be brought by or against the corporation, and not by or against the members individually.**

tain rights and privileges belonging to them by law in their aggregative capacity, were styled by the Romans 'Collegium,' and sometimes 'Universitas'; as, 'Collegia Zibicimum,' 'Collegia Aurificum,' 'Collegia Architectorum,'—the society, corporation, or community of flute players, goldsmiths, architects, etc. *Id.* bk. 20, p. 110. The terms used by one of the Roman juriconsults to describe the nature of such a corporation or associated body of individuals, under the laws of the republic, are, perhaps, as appropriate as any general language which can be used to describe a corporation aggregate at the present day, without referring to the specific object for which any particular corporation is organized. I have thus translated it from the Latin of the Digest: 'But those who are permitted to form themselves into a body, under the name of a corporation, society, or other community, have within their peculiar jurisdiction, as in the similar case of the republic, property in common, and a common chest or treasury, and an agent or head of the corporation or society, by whom, as in the republic, whatever is necessary to be done for the benefit of the community may be transacted.' *Dig. lib. 3, tit. 4a.* And from time immemorial, as at the present day, this privilege of being a corporation, or artificial body of individuals, with the power of holding their property, rights, and immunities in common, as a legally organized body, and of transmitting the same in such body by an artificial succession different from the natural successions of the property of individuals, has been considered a franchise, which could not be lawfully assumed by any associated body without a special authority for that purpose from the government or sovereign power. *Dig. lib. 47, tit. 22, De Coll. et Corp., 4 Guyol, Rep. de Jur. art. 'Communante Laique'; Domat, Pub. Law, bk. 1, tit. 15. § 2.*" *Warner v. Beers*, 23 *Wend. (N. Y.)* 103, 122. For the history of corporations, see 2 *Kent, Comm.* 268; 1 *Wat. Corp.* § 11; 1 *Pol. & M. Hist. Com. Law*, 469.

(d) A corporation may take from and convey to its members, and may contract with them, and may sue them and be sued by them.

3. That a corporation is thus a legal entity, separate and distinct from the members who compose it, is a mere legal fiction, introduced for the convenience of the corporation in transacting business, and of those who do business with it; and, when urged to an intent and purpose not within its reason and policy, it will be disregarded, and the fact that the corporation is really a collection of individuals will be recognized, even at law. Courts of equity, in numerous instances, look behind the corporate entity, and recognize the individual members, and will do so whenever justice requires.

"Persons capable of purchasing," said Lord Coke, "are of two sorts, persons natural, created of God, and persons created by the policy of man, as persons incorporated into a body politic."² The latter sort of person is what we call a corporation, or body corporate. "It is called a body corporate because the persons composing it are made into one body." "It is only in abstracto, and rests only in contemplation of law."³

Many definitions of a corporation may be found in the books, differing more or less from each other; but there are two, which are often quoted, and which bring out better than any others the two sides of a corporation. One is the definition of Chief Justice Marshall in the Dartmouth College Case; and the other is that of Mr. Kyd, who wrote on the law of corporations in England about a century ago.

Chief Justice Marshall said: "A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the

² 1 Co. Inst. 202, 250.

³ 10 Rep. 50. "A body politic is a body to take in succession, framed (as to that capacity) by policy, and therefore it is called by Littleton a 'body politic'; and it is called a 'corporation' or 'body corporate' because the persons are made into a body, and of a capacity to take and grant," etc. Co. Litt. 250a.

charter of its creation confers upon it, either expressly, or as incidental to its very existence. These are such as are supposed best calculated to effect the object for which it was created. Among the most important are immortality, and, if the expression may be allowed, individuality; properties by which a perpetual succession of many persons are considered as the same, and may act as a single individual. They enable a corporation to manage its own affairs, and to hold property without the perplexing intricacies, the hazardous and endless necessity, of perpetual conveyances for the purpose of transmitting it from hand to hand. It is chiefly for the purpose of clothing bodies of men in succession with these qualities and capacities that corporations were invented, and are in use. By these means, a perpetual succession of individuals are capable of acting for the promotion of the particular object, like one immortal being.”⁴

Mr. Kyd defines a corporation as: “A collection of many individuals united into one body, under a special denomination, having perpetual succession under an artificial form, and vested by the policy of the law with the capacity of acting in several respects as an individual, particularly of taking and granting property, of contracting obligations, and of suing and being sued, of enjoying privileges and immunities in common, and of exercising a variety of political rights more or less extensive according to the design of its institution or the powers conferred upon it, either at the time of its creation or any subsequent period of its existence.”⁵

Chancellor Kent’s description of a corporation is as follows: “A corporation is a franchise possessed by one or more individuals, who subsist, as a body politic, under a special denomination, and are vested, by the policy of the law, with the capacity of perpetual succession, and of acting in several respects, however numerous the association may be, as a single individual. The object of the institution is to enable

⁴ Per Chief Justice Marshall, in *Dartmouth College v. Woodward*, 4 Wheat. 517, 636, 1 Cumming, Cas. Priv. Corp. 490, W. D. Smith, Cas. Corp. 148, Shep. Corp. Cas. 248. “A corporation is a body, created by law, composed of individuals united under a common name, the members of which succeed each other, so that the body continues the same notwithstanding the change of the individuals who compose it, and is, for certain purposes, considered as a natural person.” Ang. & A. Corp. § 1.

⁵ 1 Kyd, Corp. 18. And see *State v. Standard Oil Co.*, 49 Ohio St. 137, 80 N. E. 279.

the members to act by one united will, and to continue their joint powers and property in the same body, undisturbed by the change of members, without the necessity of perpetual conveyances, as the rights of members pass from one individual to another. All the individuals composing a corporation and their successors are considered in law as but one person, capable, under an artificial form, of taking and conveying property, contracting debts and duties, and of enjoying a variety of civil and political rights. One of the peculiar properties of a corporation is the power of perpetual succession; for, in judgment of law, it is capable of indefinite duration. The rights and privileges of the corporation do not determine or vary on the death or change of the individual members. They continue as long as the corporation endures. * * * It was chiefly for the purpose of clothing bodies of men in succession with the qualities and capacities of one single, artificial, and fictitious being, that corporations were originally invented, and for the same convenient purpose they have been brought largely into use. By means of the corporation many individuals are capable of acting in perpetual succession like one single individual, without incurring any personal hazard or responsibility, or exposing any other property than what belongs to the corporation in its legal capacity.”⁶

In *People v. Assessors of Village of Watertown*,⁷ it was said by Bronson, J.: “A corporation aggregate is a collection of individuals united in one body, under such a grant of privileges as secures a succession of members without changing the identity of the body, and constitutes the members for the time being one artificial person, or legal being, capable of transacting some kind of business like a natural person. It does not occur to my mind that anything else can be essential to the definition. Such a union as I have mentioned can only be effected under a grant of privileges from the sovereign power of the state. A corporation is, therefore, said to be a legal being, or the mere creature of law.”

The Corporation as a Legal Entity.

These definitions show that a corporation is for many purposes, in the contemplation of law, an artificial person or entity, having an individuality separate and distinct from that of the members who compose it. The existence of the members is, in law, and, for most pur-

⁶ 2 Kent, Comm. 267, 268.

⁷ 1 Hill (N. Y.) 620.

poses, in equity also, merged in that of the corporate body, and lost sight of. As a legal entity it takes and holds property, and conveys the same; it contracts obligations, and it sues and is sued, in its corporate name, in the same manner as a natural person. For these purposes the members of the corporation are not regarded. Their existence is merged in that of the corporate body. They compose the corporation, but they are not the corporation.⁸

In an English case, which serves as a good illustration of this characteristic of a corporation, suit was brought to compel customhouse officers to register a vessel belonging to a British corporation, and was resisted on the ground that, as some of the members of the corporation were foreigners, the vessel did not belong wholly to British subjects, as was required by statute to entitle it to registry. The court held, however, that the vessel belonged to the corporation, and not to the individual members, and was therefore entitled to registry, and that this would be so even if all the stock in the corporation had been owned by foreigners.⁹

This characteristic of a corporation, as a legal entity, separate and distinct from its members, is very important, and is of peculiar importance with respect to the ownership and conveyance of corporate property, the effect of corporate contracts, and the right to maintain actions concerning corporate property and rights, and for corporate wrongs. For these purposes the law generally considers the corporate body only.¹⁰ The members of a corporation do not take, nor can they grant, its property; but the corporation does so itself in its corporate name. The corporate property does not in any legal sense vest in or belong to the individual members, though they are interested in it to the extent that they may derive benefit from its increase, or suffer loss from its destruction.* They are in no legal sense, however, the owners of its property. As we have seen, for instance, property belonging

⁸ See *The Queen v. Arnaud*, 16 Law J. C. L. 50, 1 Cumming, Cas. Priv. Corp. 30; *Smith v. Hurd*, 12 Metc. (Mass.) 371, 1 Cumming, Cas. Priv. Corp. 792; *Bronson, J.*, in *People v. Assessors of Village of Watertown*, 1 Hill (N. Y.) 620; and the cases cited in the following notes.

⁹ *The Queen v. Arnaud*, *supra*.

¹⁰ *Post*, p. 389.

*Present ownership not being necessary to give an insurable interest in property, it has been held that a stockholder has such a beneficial interest in the corporate property as to give him an insurable interest. *Warren v. Insurance Co.*, 31 Iowa, 464.

to a British corporation belongs wholly to a British subject (the corporation), though some or even all of its members may be foreigners.¹¹ So, a member of a corporation has not such a distinct right in its property as to make his interest attachable for his debts.¹² And the corporation, and not the individual members, must bring trover for conversion of its property,¹³ or replevin to recover possession of the same.¹⁴ And the members of a corporation have no power to sell or convey its property, but all such transactions must be by and in the name of the corporation.¹⁵ The members of a corporation cannot bind it by contracts entered into individually. A corporation, as we shall see, may become bound by a contract entered into on its behalf by its promoters, by adopting it, or accepting the benefit of it; but here the corporation, by adoption, makes a contract itself. Contracts made by the members of a corporation as individuals, either before or after incorporation, do not bind the corporation.¹⁶ Nor can the declarations or admissions of individual members of a corporation, when they are not authorized to act as its agent in the matter, be received as evidence against the corporation, any more than the declarations and admissions of a stranger could be admitted.†

¹¹ *The Queen v. Arnaud*, *supra*.

¹² *Williamson v. Smoot*, 7 Mart. (La.) 34, 1 Cumming, Cas. Priv. Corp. 32.

¹³ *Tomlinson v. Bricklayers' Union*, 37 Ind. 308, 1 Cumming, Cas. Priv. Corp. 38.

¹⁴ *Button v. Hoffman*, 61 Wis. 20, 20 N. W. 667, 1 Cumming, Cas. Priv. Corp. 38.

¹⁵ *Wheelock v. Moulton*, 15 Vt. 519, 1 Cumming, Cas. Priv. Corp. 35; *Baldwin v. Canfield*, 26 Minn. 43, 1 N. W. 261; *Parker v. Hotel Co.* (Tenn. Sup.) 34 S. W. 209; *Humphreys v. McKissock*, 140 U. S. 304, 11 Sup. Ct. 779.

¹⁶ *Davis v. Creamery Co.* (Neb.) 67 N. W. 438. In *Moore & Handley Hardware Co. v. Towers Hardware Co.*, 87 Ala. 206, 6 South. 41, a valid contract was entered into by competing firms, by which one of them agreed not to sell goods in a certain territory in opposition to the other. After this the members of this firm and others formed a corporation for carrying on the same general business, and after a time announced their intention to handle the same goods formerly sold by the firm, and in the district in which the firm had bound themselves not to sell. It was held that, in the absence of allegations that the corporation was fraudulently created with the intent on the part of the stockholders to evade and avoid their obligations as individuals, and that the partners in the original firm had reserved to themselves interests in the business distinct from their interests as stockholders, the corporation could not be enjoined from carrying on the business.

† *Polleys v. Insurance Co.*, 14 Me. 141; *Fairfield County Turnpike Co. v. Thorp*, 18 Conn. 173.

These rules are the same even when all the stock in the corporation is owned by one person, for this circumstance does not change his relation as a mere stockholder. The corporation is still a separate and distinct artificial person, in the eye of the law.¹⁷

On the same principle, the shares in a corporation organized for the sole purpose of holding and managing real estate, are personal property, and not real estate. The members do not own the real estate. It is owned by the corporation, the artificial being, and not in any sense by the individual members, like partnership real estate, which is owned by the partners as tenants in common.¹⁸

It also follows from the distinction between the individuality of the corporation and that of its members that a corporation may convey its property to one or more of its members, or its members may convey to it, and it may enter into contracts with its members, without the conveyance being open to the objection that the same person is both grantor and grantee, or the contract being objectionable on the ground that it is a contract by a man with himself.¹⁹

It also follows from this characteristic of corporate bodies that a corporation may sue its members, and be sued by them.²⁰ So, actions by and against corporations are not in any sense actions by and against the stockholders. Thus, a sheriff, who owns stock in a corporation, is not a party to a suit by or against the corporation, within the meaning of a statute disqualifying an officer from serving process where he is a party to the suit.²¹ For the same reason, a justice or

¹⁷ "The owner of all the capital stock of a corporation does not, therefore, own its property, or any of it, and does not himself become the corporation, as a natural person, to own its property and do its business in his own name. While the corporation exists, he is a mere stockholder of it, and nothing else." *Button v. Hoffman*, *supra*. And see *Wheelock v. Moulton*, *supra*; *Baldwin v. Canfield*, *supra*; *Parker v. Hotel Co.*, *supra*. In this case it was held that a stockholder of a corporation does not, by becoming owner of the entire stock, acquire an equitable estate in real property of the corporation which would enable him to make a conveyance thereof in his own name. But see *Bundy v. Iron Co.*, 38 Ohio St. 300.

¹⁸ *Russell v. Temple* (Mass.) 3 Dane, Abr. 108.

¹⁹ *Pope v. Brandon*, 2 Stew. (Ala.) 401; *Foster v. Commissioners of Inland Revenue* [1894] 1 Q. B. 516; *Lexington Life, F. & M. Ins. Co. v. Page*, 17 B. Mon. (Ky.) 412; *Gordon v. Preston*, 1 Watts (Pa.) 385; *post*, pp. 253 et seq., 504.

²⁰ *Waring v. Catawba Co.*, 2 Bay, (S. C.) 109; *Pope v. Brandon*, *supra*; *Culbertson v. Navigation Co.*, Fed. Cas. No. 3,464; *Geer v. School Dist.*, 6 Vt. 76; *Sawyer v. Society*, 18 Vt. 405; *Rogers v. Society*, 19 Vt. 187.

²¹ *Merchants' Bank v. Cook*, 4 Pick. (Mass.) 405.

judge who is related to a member of a corporation, or who is himself a member, is not disqualified to try an action by or against the corporation, under a statute disqualifying because of relationship to either of the "parties."²² And in a late Minnesota case it was held that the demands of stockholders individually cannot be interposed as equitable set-offs to a demand against the corporation, even though the plaintiff be insolvent.²³ The federal courts are given jurisdiction in certain cases of suits between citizens of different states. Within the meaning of the law, a corporation is a citizen of the state of its creation, and may sue a citizen of another state, though all of its members may be citizens of the latter state. The action is by the corporation, not by its members.²⁴

The Corporation as a Collection of Individuals.

When it is thus said that a corporation is a legal entity, separate and distinct from the persons who compose it,—that the individual existence of the members is merged in the artificial individuality of the corporate body,—it must not be understood that the law cannot under any circumstances look behind this artificial entity, and notice the existence and acts of its members. One cannot shut his eyes to the fact that private corporations are all formed by an association of individuals, under authority of law, and that to this extent they are mere collections of individuals. The legal conception of a corporation as an entity distinct from its members is a mere fiction adopted by the law, for the purpose of enabling natural persons to transact business in this peculiar way; and, whenever it is necessary to do so, the law will look behind the corporate body, and recognize the members, and disregard the fiction.

In a late New York case,²⁵ the state asked a forfeiture of the charter of a corporation because of its illegal conduct in entering into an unlawful association with other corporations and firms engaged in the same business. There had been no formal action by the defendant's trustees or directors, but the stockholders individually

²² *Searsburgh Turnpike Co. v. Cutler*, 6 Vt. 315; *Steuart v. Bank*, 19 Johns. (N. Y.) 501. Contra, *Washington Ins. Co. v. Price*, 1 Hopk. Ch. (N. Y.) 1.

²³ *Gallagher v. Brewing Co.*, 53 Minn. 214, 54 N. W. 1115.

²⁴ *Post*, p. 74.

²⁵ *People v. North River Sugar-Refining Co.*, 121 N. Y. 582, 24 N. E. 834. See, also, *People v. Kingston & M. Turnpike Road Co.*, 23 Wend. (N. Y.) 193.

had transferred their stock to the parties representing the combination. It was contended that the combination was due to the acts of the stockholders, and not to any corporate action, and that, therefore, the corporation was not guilty of any misconduct. The court declined to take this view, and held that the misconduct of the stockholders, and of the officers in recognizing the transfers of stock, was the misconduct of the corporation.²⁶ A like question arose in a late Ohio case, and a like decision was made.²⁷

²⁶ It was said in this case: "There may be actual corporate conduct which is not formal corporate action; and where that conduct is directed or produced by the whole body, both of officers and stockholders, by every living instrumentality which can possess and wield the corporate franchise, that conduct is of a corporate character, and, if illegal and injurious, may deserve and receive the penalty of dissolution. * * * The abstract idea of a corporation, the legal entity, the impalpable and intangible creation of human thought, is itself a fiction, and has been appropriately described as a figure of speech. It serves very well to designate in our minds the collective action and agency of many individuals as permitted by the law; and the substantial inquiry always is what in a given case has been that collective action or agency. As between the corporation and those with whom it deals, the manner of its exercise usually is material; but, as between it and the state, the substantial inquiry is only what that collective action and agency has done, what it has, in fact, accomplished, what is seen to be its effective work, what has been its conduct. It ought not to be otherwise. The state gave the franchise, the charter, not to the impalpable, intangible, and almost nebulous fiction of our thought, but to the corporators, the individuals, the acting and living men, to be used by them, and redound to their benefit, to strengthen their hands, and add energy to their capital. If it is taken away, it is taken from them as individuals and corporators, and the legal fiction disappears. The benefit is theirs, the punishment is theirs, and both must attend and depend upon their conduct; and when they all act collectively, as an aggregate body, without the least exception, and, so acting, reach results and accomplish purposes clearly corporate in their character, and affecting the vitality, the independence, the utility, of the corporation itself, we cannot hesitate to conclude that there has been corporate conduct which the state may review, and not be defeated by the assumed innocence of a convenient fiction."

²⁷ *State v. Standard Oil Co.*, 49 Ohio St. 137, 30 N. E. 279. In this case it was said: "The general proposition that a corporation is to be regarded as a legal entity, existing separate and apart from the natural persons composing it, is not disputed; but that the statement is a mere fiction, existing only in idea, is well understood, and not controverted by any one who pretends to accurate knowledge on the subject. It has been introduced for the convenience of the company

Courts of equity, in numerous instances, look behind the corporation, and recognize the rights of the corporation as being in reality rights of the individuals composing it. The rights of the members of a corporation, in their collective capacity, in its property, must generally be enforced, even in equity, through the corporation as a distinct legal person; but if, for any reason, this cannot be done, courts of equity will not allow the legal fiction of a distinct corporate entity to stand in the way of justice. Thus, though an action against the officers of a corporation for conversion of its property, or a suit in equity to enjoin them, must be brought in the name of the corporation if it can be done, yet, if the offending officers are a majority of the directors, and own a majority of the stock, so that an injured stockholder cannot obtain relief at law through the corporation, he may maintain a suit in equity in his own name.²⁸ On the other hand, if all the stockholders of a corporation are individually in such a position as to be without equity in regard to a particular matter, they cannot obtain equitable relief through the corporation, and in its name.²⁹

CREATION OF CORPORATIONS.

4. A corporation can only be created by or under authority from the state. It cannot be formed by mere agreement between the members.

in making contracts, in acquiring property for corporate purposes, in suing and being sued, and to preserve the limited liability of the stockholders by distinguishing between the corporate debts and property of the company and of the stockholders in their capacity as individuals. All fictions of law have been introduced for the purpose of convenience, and to subserve the ends of justice. It is in this sense that the maxim, 'In fictione juris subsistit æquitas,' is used, and the doctrine of fictions applied. But, when they are urged to an intent and purpose not within the reason and policy of the fiction, they have always been disregarded by the courts. * * * Now, so long as a proper use is made of the fiction that a corporation is an entity apart from its shareholders, it is harmless, and, because convenient, should not be called in question; but, where it is urged to an end subversive of its policy, * * * the fiction must be ignored."

²⁸ Post, p. 389.

²⁹ *Arkansas River Land, Town & Canal Co. v. Farmers' Loan & Trust Co.*, 13 Colo. 587, 22 Pac. 954.

In this respect a corporation is very different from an ordinary partnership. A partnership is formed by a mere agreement between the parties who become members, and no legislative authority at all is necessary. A corporation cannot be so formed. It can only be created by or under authority from the state conferred by the legislature. The creation of corporations will be considered at length in a subsequent chapter.⁸⁰

LIMITED POWERS OF CORPORATIONS.

5. A corporation, being the mere creature of the legislature, has such powers only as are expressly or impliedly conferred upon it by the charter or act of incorporation.

A common partnership has the same powers as the members would have individually. As its formation does not depend at all upon legislative authority, neither do its powers. A corporation, on the other hand, being the creature of the legislature, has such powers, and such powers only, as are expressly or impliedly conferred upon it by the charter or act of incorporation. It cannot do acts which would be lawful for individuals, or even praiseworthy, unless the power to do them can be derived from its charter.⁸¹

ATTRIBUTES AND INCIDENTS OF A CORPORATION.

6. The following powers and faculties, and these only, are essential to the existence of a corporation:
- (a) To have continuous succession, under a special name, and in an artificial form, without being subject to dissolution or change of identity by the death, withdrawal, or legal disability of individual members.
 - (b) To take and grant property and contract obligations, within the limits of the power conferred upon it by its charter, and to sue and be sued, in its corporate name, in the same manner as an individual.

⁸⁰ Post, p. 33.

⁸¹ Post, p. 120.

- (c) To receive grants of privileges and immunities, and to enjoy them in common.

7. The following powers and faculties are incident to most private corporations, but are not essential to corporate existence:

- (a) Transferability of shares.
- (b) Exemption of the members from personal liability for the debts of the corporation beyond the amount of their respective proportions of the capital.
- (c) Power to purchase and hold real estate.
- (d) Power to use a common seal.
- (e) Power to make by-laws.

8. The distinguishing characteristic of a corporation, "which makes it to be such, and not some other thing, in legal contemplation, is the merging of the individuals composing the aggregate body into one distinct, artificial, individual existence."

Under this head we shall ascertain the attributes and incidents of a corporation, and the characteristics which distinguish it from other associations of individuals. A corporation is known to the law by the powers and faculties bestowed upon it, expressly or impliedly, by the charter or act creating it. The words "corporation" or "incorporate" need not be used in its creation.³² Nor, on the other hand, does the use of such words necessarily make the particular association a corporate body. The use of these or equivalent words may impliedly confer corporate powers and faculties, and therefore create a corporation, if there is nothing to show that powers and faculties essential to corporate existence were intended to be withheld; but if, in fact, essential powers and faculties are not conferred, then the body created or intended to be created is no corporation, whatever may have been the intention of the legislature. On the other hand, even the express declaration of the legislature,

³² Thomas v. Dakin, 22 Wend. (N. Y.) 9, 1 Cumming, Cas. Priv. Corp. 1; Sutton's Hospital Case, 10 Coke, 28a, 28a, 2 Cumming, Cas. Priv. Corp. 14, Shep. Cas. Corp. 3; Conservators of the River Tone v. Ash, 10 Barn. & C. 349, 1 Cumming, Cas. Priv. Corp. 23; Blanchard v. Kaul, 44 Cal. 440.

in the act by which it creates or authorizes an association, that it shall not constitute or be considered a corporation, will not prevent the courts from holding that it is a corporation, if the attributes conferred upon it make it so.³³ In order, therefore, to determine whether a particular association is a corporation or not, it is necessary to ascertain the properties essential to constitute such a body, and compare them with those conferred upon the association. If they exist in common or substantially correspond, the association is a corporation; otherwise, it is not.³⁴ As we shall see, many faculties are generally incident to a corporation, but are not essential to corporate existence. And, on the other hand, some faculties which are essential may exist also in an unincorporated association.

The powers and faculties generally specified as creating corporate existence are: (1) The capacity of perpetual succession; (2) the power to grant and receive, to contract, and to sue and be sued, in the corporate name; (3) the power to purchase and hold real and personal estate; (4) the power to have a common seal; and (5) the power to make by-laws. As was pointed out in a New York case,³⁵ however, these indicia were given by judges and elementary writers at a very early day. Since that time the institutions have greatly multiplied, their practical operation and use have been thoroughly tested, and their peculiar and essential properties much better understood, and at the present time some of the powers above specified are wholly unessential.

³³ Bronson, J., in *People v. Assessors of Village of Watertown*, 1 Hill (N. Y.) 620; Hand, Senator, in *Gifford v. Livingston*, 2 Denio (N. Y.) 395; *Liverpool Ins. Co. v. Massachusetts*, 10 Wall. 566, 1 Cumming, Cas. Priv. Corp. 26, W. D. Smith, Cas. Corp. 13, Shep. Cas. Corp. 5. In the latter case an association created by the British parliament was expressly declared not to be a corporation, but it was given all the attributes necessary to make it one. It was held by the supreme court of the United States that, whatever might be the effect of such declaration in the British courts, it could not alter the essential nature of a corporation, or prevent the courts of another jurisdiction from inquiring into its true character, whenever it should come in issue; and it was held that the body was a corporation.

³⁴ *Thomas v. Dakin*, *supra*; *Sutton's Hospital Case*, *supra*; *Conservators of the River Tone v. Ash*, *supra*; *Liverpool Ins. Co. v. Massachusetts*, *supra*.

³⁵ *Thomas v. Dakin*, *supra*.

Perpetual Succession.

One of the chief attributes of a corporation, and one that is essential to corporate existence, is the power or faculty of having perpetual succession,³⁶ under a special denomination, and in an artificial form, without being subject to dissolution or change of identity by reason of the death, legal disability, or withdrawal of members. In the case of an ordinary partnership, the withdrawal of a member dissolves the firm. Even if the remaining partners continue to carry on the business as a firm, and under the same firm name, the identity of the firm is changed. The remaining partners constitute a new and distinct firm. Even if the outgoing partner transfers his interest with the consent of the other members, so as to introduce the transferee into the partnership, there is, in law, a new partnership agreement, and a new firm. However numerous such changes in membership may be, and though there may be no break in the continuity of the business, nor change in the firm name, at each change an existing firm is dissolved, and a new one is formed.³⁷ So, where a partner dies, this will ordinarily dissolve the firm, and his interest in the property will go to his heirs and personal representatives. And there are some legal disabilities, which, if they attach to a partner, will operate as a dissolution of the firm.³⁸

This is not true of a corporation. Neither the existence of a corporation nor its identity is in any way affected or changed by the withdrawal of individual members. Unless prevented by the peculiar nature and object of the corporation,³⁹ any member may trans-

³⁶ It is generally said, as in the text, that a corporation has the faculty of "perpetual" succession, and a corporation has been described as an "immortal" being. It is not meant by this that a corporation must, but simply that it may, continue forever. Private corporations are almost always limited in their duration, by the act creating them, to a certain number of years; and, even when not so limited, they may forfeit their right to corporate existence, and be dissolved.

³⁷ 17 Am. & Eng. Enc. Law, 1093. It is permissible, it has been said, for parties to stipulate in a partnership agreement that the death of a member of the firm or an assignment by him of his interest shall not dissolve the partnership, but that the executors of the deceased partner or his assignee, as the case may be, shall succeed to membership. *Warner v. Beers*, 23 Wend. (N. Y.) 103, 146, 1 Cumming, Cas. Priv. Corp. 10, W. D. Smith, Cas. Corp. 3. Even in such a case as this, however, the identity of the firm is necessarily changed.

³⁸ 17 Am. & Eng. Enc. Law, 1102-1107.

³⁹ Post, p. 18.

fer his shares without the consent of his associates, and the transferee will come into the association as a member, without in any sense changing the identity or affecting the existence of the corporate body.⁴⁰ So, if a member dies, the existence or identity of the corporation is not affected; but whoever becomes the legal holder of the shares, which are transferred by operation of law like other personal property, succeeds to membership. This mark of corporate existence may exist in unincorporated associations by statute.⁴¹

The Faculty of Acting as a Legal Entity.

An essential attribute of a corporation is the power or faculty of acting as a legal entity. This attribute has already been explained at some length.⁴² We have seen that a corporation can take and grant property and contract obligations within the limits authorized by its charter, and sue and be sued, in its corporate name, in the same manner as an individual. In other words, it has the faculty of dealing and being dealt with as a distinct person in the eye of the law, apart from its members. In this respect a corporation differs widely from an ordinary partnership. If a firm takes a conveyance of property, it vests in the partners individually as tenants in common, each having an undivided interest therein. And each member of the firm may by his individual act transfer his interest in the firm property. When a firm enters into a contract, it is a joint contract, binding the partners as individuals. When suit is brought by or against a firm, it must, in the absence of statutory provision to the contrary, be brought by or against the members individually. In a word, the common law does not recognize a firm as a legal entity apart from the members, but deals with the members themselves individually.

It is altogether different in the case of a corporation. Such a body is for many purposes a legal entity, separate and distinct from its members. They compose the corporation, but in law they are not the corporation. A corporation, in the exercise of its power to take and grant property, to enter into contracts, etc., acts through its agents as an individual. Being impersonal, it can only act by means of duly-appointed agents. But the acts of the agents are in law the acts of the corporation, and not the acts of the individual members. So, when a cause of action accrues in favor of or against a corporation, the

⁴⁰ Post, p. 18.

⁴¹ Post, p. 23.

⁴² Ante, p. 5.

corporate body sues or is sued in its corporate name, and the suit is not brought by or against the members individually.⁴³

Special Denomination, or Corporate Name.

A name is essential to a corporation, for without a name it could not be known, it could not contract, it could not make or take a conveyance of property, it could not sue or be sued; in short, it could do no act as an artificial person distinct from its members. "A corporation is a body politic, consisting of material bodies, which, joined together, must have a name to do things which concern the corporation, or else it is no corporation."⁴⁴

The right to use a special name, to contract obligations under it, and the right and liability to sue and be sued by it, has been mentioned as a criterion of corporate existence; but it is not so. Unincorporated associations may be authorized by statute to use a special name, and to sue and be sued by it; and, by statute, in some states, a limited partnership may sue and be sued in the name of the general partner.

⁴³ Ante, p. 5, where this attribute of a corporation is explained at length.

⁴⁴ *Conservators of the River Tone v. Ash*, 10 Barn. & C. 349, 1 Cumming, Cas. Priv. Corp. 23. And see *Mariot v. Mascal*, And. 206; post, p. 71. The fact that an association having all the essential attributes of a corporation conducts part of its business in its corporate name, and part in the name of its president for the time being,—as where it contracts in its corporate name, and sues and is sued in the name of its president,—in no degree changes the character of the body, for a corporation may have more than one name. "A corporation may have more than one name. It may have one in which to contract, grant, etc., and another in which to sue and be sued. So, it may be known by two different names, and may sue and be sued in either; and the name of the president, his official name, or any other, will answer every purpose. The only material circumstance is a name or names of some kind in which all the affairs of the company may be conducted." *Thomas v. Dakin*, 22 Wend. (N. Y.) 9, 1 Cumming, Cas. Priv. Corp. 1; *Liverpool Ins. Co. v. Massachusetts*, 10 Wall. 566, 1 Cumming, Cas. Priv. Corp. 26, W. D. Smith, Cas. Corp. 13, Shep. Cas. Corp. 5. In these cases the statute provided for suits by and against the associations in the name of their principal officer, and the associations were allowed to contract in their artificial name. It was held that they were corporations. "If it can contract in the artificial name," it was said in the case last cited, "and sue and be sued in the name of its officers on those contracts, it is in effect the same, for process would have to be served on some such officer even if the suit were in the artificial name."

Transferability of Shares.

In the case of a partnership, a member of the firm cannot, unless there is a provision therefor in the partnership articles, transfer his membership to another, without the consent of the other members. In the case of most private corporations, on the other hand, the shares are transferable without the consent of the other shareholders.⁴⁵ Transferability of shares has been mentioned as one of the distinguishing features of a corporation, but it is not necessarily so. It is an incident of most private corporations, but it is by no means essential to corporate existence. For instance, it does not enter into the constitution of chartered colleges, academies, hospitals, and other corporate institutions founded by public endowment or private beneficence; nor of incorporated scientific and literary societies, or corporate societies for mutual benefit or charity, in the funds of which the members have a beneficial interest, such as mutual benefit insurance companies, trade unions, etc. The absence of this feature, therefore, does not show that the particular association is not a corporation. Nor, on the other hand, does the fact that shares are transferable show that the association is a corporate body, for the right to transfer may, if the parties choose, be provided for in partnership articles.⁴⁶ There is this difference, however. In most private corporations the transferability of shares is incidental, and need not be expressly provided for. In the case of a partnership an express provision is necessary to render the shares transferable.

Exemption of Members from Personal Liability.

One of the most familiar distinctions, in general and popular understanding, between corporate bodies and common partnerships or other unincorporated associations, is the exemption of the members from personal liability for the debts of the association. In the case of a partnership, at common law, each member is personally liable for all the debts of the firm, after the joint assets have been exhausted. In the case of a corporation, at common law, the members of a business corporation are exempt from personal liability for the debts of the corporation beyond the amount of their respective proportions of the capital.

⁴⁵ Post, p. 406.

⁴⁶ Warner v. Beers, 23 Wend (N. Y.) 103, 1 Cumming, Cas. Priv. Corp. 10; W. D. Smith, Cas. Corp. 3.

This has often been mentioned as peculiar to a private corporation, but it is not necessarily so. The exemption of members from personal liability is merely an incident to a corporation, in the absence of a statute altering the common-law rule. It is not an essential attribute. In most states statutes have been enacted, rendering the members of a private business corporation personally liable, to a greater or less extent, for its debts, where the corporate assets are insufficient to pay them in full. Such a statute does not in any sense change the character of the body as a corporation.⁴⁷ On the other hand, the liability of partners may be thus limited. The statutes relating to limited partnerships show that the partners may be exempted from liability beyond their shares in the joint fund, without converting such firms into bodies corporate. Besides this, persons have a natural right, unless restrained by legislative enactment, to contract to make payment only to the amount of certain specific funds.⁴⁸

Power to Purchase and Hold Real Estate.

Among the other powers which are usually attributed to corporations, but which are by no means essential to corporate existence, may be mentioned the power to purchase and hold real estate. This power generally exists, but it is altogether unessential, unless the purpose for which the corporation was created requires it to hold real estate.

Power to Use a Common Seal.

So it is with the power to use a common seal. At common law a corporation has, as an incident, the power to use a seal whenever it is necessary in the transaction of its business; but the power may be dispensed with altogether, for it is well settled that corporations may, unless expressly restricted by their charter, contract by resolutions, or through agents, and without a seal.⁴⁹

⁴⁷ Warner v. Beers, *supra*; Liverpool Ins. Co. v. Massachusetts, 10 Wall. 566, 1 Cumming, Cas. Priv. Corp. 26, W. D. Smith, Cas. Corp. 13, Shep. Cas. Corp. 5. See post, p. 564.

⁴⁸ Warner v. Beers, *supra*.

⁴⁹ Post, p. 156; dictum of Nelson, C. J., in Thomas v. Dakin, 22 Wend. (N. Y.) 9, 1 Cumming, Cas. Priv. Corp. 1.

Right to Make By-Laws.

The same may be said of the right to make by-laws. This power is generally incidental to a corporation, but it is not essential to corporate existence. It is unnecessary in all cases where the charter sufficiently provides for the government of the body.⁵⁰

Conclusion as to Attributes Essential to Corporate Existence.

In a leading New York case, it was said by Chief Justice Nelson: "The distinguishing feature [of a corporate body], far above all others, is the capacity conferred, by which a perpetual succession of different persons shall be regarded in the law as one and the same body, and may at all times act, in fulfillment of the objects of the association, as a single individual. In this way a legal existence, a body corporate, an artificial being, is constituted, the creation of which enables any number of persons to be concerned in accomplishing a particular object, as one man. While the aggregate means and influence of all are wielded in effecting it, the operation is conducted with the simplicity and individuality of a natural person. In this consists the essence and great value of these institutions. Hence it is apparent that the only properties that can be regarded strictly as essential are those which are indispensable to mold the different persons into this artificial being, and thereby enable it to act in the way above stated. When once constituted, the powers and faculties that may be conferred are various,—limited or enlarged, at the discretion of the legislature, and will depend upon the nature and object of the institution, which is as competent as a natural person to receive and enjoy them. We may, in short, conclude by saying, with the most approved authorities at this day, that the essence of a corporation consists in a capacity (1) to have perpetual succession under a special name, and in an artificial form; (2) to take and grant property, contract obligations, sue and be sued, by its corporate name as an individual; and (3) to receive and enjoy in common grants of privileges and immunities."⁵¹

⁵⁰ Post, p. 454; *Thomas v. Dakin*, *supra*.

⁵¹ *Thomas v. Dakin*, 22 Wend. (N. Y.) 9, 1 Cumming, Cas. Priv. Corp. 1. To the same effect, see 1 Kyd, Corp. 70; *Southern Pac. R. Co. v. Orton*, 32 Fed. 457, 473.

The Distinguishing Characteristic of a Corporation.

As we have seen in the preceding pages, many of the incidents of a corporation are not essential, and many of the essential attributes may also exist in the case of a common partnership or unincorporated joint-stock association. It is important, therefore, to find some characteristic of corporations that can be relied upon as a distinguishing mark. The only feature that can be thus relied upon is the existence of the corporation as an entity separate and distinct from the members who compose it. "The most peculiar and strictly essential characteristic of a corporate body, which makes it to be such, and not some other thing, in legal contemplation, is the merging of the individuals composing the aggregate body into one distinct, artificial individual existence."⁵²

Unincorporated Joint-Stock Companies.

A joint-stock company is an unincorporated association of individuals for business purposes, resembling an ordinary partnership in many respects, but which, unlike an ordinary partnership, has a common fund or capital stock, divided into shares, which are apportioned among the members in proportion to their respective contributions, and which are assignable by the owner without the express consent of the other members. "The words 'joint-stock company' have never been used as descriptive of a corporation created by special act of the legislature, and authorized to issue certificates of

⁵² Per Verplanck, Senator, in *Warner v. Beers*, 23 Wend. (N. Y.) 108, 1 Cumming, Cas. Priv. Corp. 5, W. D. Smith, Cas. Corp. 3. In *Liverpool Ins. Co. v. Massachusetts*, 10 Wall. 566, 1 Cumming, Cas. Priv. Corp. 26, W. D. Smith, Cas. Corp. 13, Shep. Cas. Corp. 5, the question arose whether a British insurance company was a corporation or not, within the meaning of a Massachusetts statute imposing a tax on foreign corporations. The supreme court of the United States, after pointing out that the company had a distinctive and artificial name by which it could make contracts; that there was a statutory provision by which it could sue and be sued in the name of one of its officers as the representative of the whole body, which would be bound by the judgment rendered in such suit; that there was a provision for perpetual succession by the transfer and transmission of the shares of its capital stock, whereby new members might be introduced in the place of those who might die or sell out; that its existence as an entity separate and apart from the shareholders was recognized by the act of parliament in enabling it to sue its shareholders, and be sued by them,—held that these attributes made the body a corporation, notwithstanding the act of parliament creating it declared that it should not be so regarded.

stock to its shareholders. They describe a partnership made up of many persons acting under articles of association, for the purpose of carrying on a particular business, and having a capital stock, divided into shares transferable at the pleasure of the holder."⁵³ These associations are nothing but partnerships, and, except in so far as the legislature has conferred special rights and privileges upon the members, they are subject to all the liabilities of partners.⁵⁴ Both in England and in this country statutes have been enacted conferring upon joint-stock companies many faculties possessed by corporations, and for this reason the resemblance between corporations and joint-stock companies is very close. It is often difficult to distinguish them. The distinction, however, is important.

Joint-stock companies are formed solely by agreement between the associates, and rest upon their common-law right to contract with each other, and do not depend at all, as in the case of a corporation, upon license or authority from the state. They are merely a peculiar kind of partnership.⁵⁵

They do not act like a common partnership, in which each partner is the agent of the others in conducting the firm business; but they generally act by a board of trustees or directors, like a corporation, the shareholders having no power to bind the other members.⁵⁶

It is generally provided by statute that, when a cause of action

⁵³ *Attorney General v. Mercantile Marine Ins. Co.*, 121 Mass. 524, 528.

⁵⁴ *Hedge & Horn's Appeal*, 63 Pa. St. 273, where it is said that a joint-stock company is a partnership, the capital of which is divided into shares, so as to be transferable without the express consent of all the co-partners. And see *Hoadley v. County Com'rs*, 105 Mass. 519, 526. And see *Butterfield v. Beardsley*, 28 Mich. 412; *Wells v. Gates*, 18 Barb. (N. Y.) 554; *Rickart v. People*, 79 Ill. 85.

⁵⁵ *People v. Coleman*, 133 N. Y. 279, 31 N. E. 96, and 2 Cumming, Cas. Priv. Corp. 2; *Hoadley v. County Com'rs*, 105 Mass. 519, 526.

⁵⁶ *Burnes v. Pennell*, 2 H. L. Cas. 520; *Bray v. Farwell*, 81 N. Y. 600. The reason that each member of a common partnership may thus bind the others is because, by carrying on the business jointly as a firm, the members hold out to the world that each has authority to manage the partnership concerns. It could be stipulated, however, even in an ordinary partnership agreement, that only a certain member shall have authority to bind the firm, and such a stipulation would be effectual as against all persons with notice of it. Since a joint-stock company notoriously conducts its business only through its board of trustees or directors, the members, as such, have no power to bind it. Every person has notice of this. *Burnes v. Pennell*, *supra*.

accrues in favor of or against a joint-stock company, action may be brought by or against it in the name of a certain officer. In the absence of such a provision, all the members would have to be made parties as in the case of an ordinary partnership.⁵⁷

As a joint-stock company is a partnership, the members, however numerous, are subject to all the ordinary liabilities of partners, except in so far as their liability may be limited by agreement or by statute. They must generally be sued as partners, and each member is personally liable for all the debts of the company after the joint assets are exhausted.⁵⁸ This liability, however, may be limited by statute, or even by agreement between the associates if known to the person dealing with the company, without changing the company into a corporation. And, as has been seen, members of a corporation may, by statute, be made liable for its debts.⁵⁹

As shown above, the shares in a joint-stock company are transferable by the holder without the consent of his associates. So, on the death of the holder, they may pass like other property. These associations, therefore, have the faculty of succession.⁶⁰

How, then, it may well be asked, are we to always distinguish such an association from a corporation? The New York court has held that the distinction is in the fact "that the creation of the corporation merges in the artificial body, and drowns in it the individual rights and liabilities of the members, while the organization of a joint-stock company leaves the individual rights and liabilities unimpaired and in full force."⁶¹ "A joint-stock company," it has been said, "is a partnership, with some of the powers of a corporation."⁶²

⁵⁷ *Williams v. Bank*, 7 Wend. (N. Y.) 539, 542.

⁵⁸ *Taft v. Ward*, 106 Mass. 518; *Tappan v. Bailey*, 4 Metc. (Mass.) 529; *Tyrrell v. Washburn*, 6 Allen (Mass.) 466; *Boston & A. R. Co. v. Pearson*, 128 Mass. 445; *Frost v. Walker*, 60 Me. 468; *Wells v. Gates*, 18 Barb. (N. Y.) 554; *Butterfield v. Beardsley*, 28 Mich. 412; *Robbins v. Butler*, 24 Ill. 387.

⁵⁹ Ante, p. 19.

⁶⁰ See *Burnes v. Pennell*, 2 H. L. Cas. 520; *Tenney v. Protective Union*, 37 Vt. 64; *Willis v. Chapman* (Vt.) 85 Atl. 459.

⁶¹ *People v. Coleman*, 133 N. Y. 279, 31 N. E. 96, and 2 Cumming, Cas. Priv. Corp. 2. And see *Warner v. Beers*, 23 Wend. (N. Y.) 103, 1 Cumming, Cas. Priv. Corp. 5, *W. D. Smith, Cas. Corp.* 3.

⁶² *People v. Coleman*, supra. In this case it was said: The distinction between a corporation and an unincorporated joint-stock association is "that the creation

CORPORATION AS A "PERSON," "CITIZEN," ETC.

9. When the reason and design of a statutory or constitutional provision, reserving or conferring a right or remedy, or imposing a duty or liability, upon "persons," "citizens," "inhabitants," etc., applies to corporations, they are within the scope of the statute or constitution, though not specially referred to.

A corporation, though a collection of individuals, has, as we have seen, a separate and distinct individuality. Though it is an artificial being, a mere creature of the legislature, it is in law a person,—an arti-

of the corporation merges in the artificial body, and drowns in it the individual rights and liabilities of the members, while the organization of a joint-stock company leaves the individual rights and liabilities unimpaired and in full force.

* * * The drift of legislation has been to lessen and obscure the original and characteristic difference. On the one hand, corporations have been created with positive provisions retaining more or less the individual liability of the members; and, on the other, the joint-stock companies have been clothed with most of the corporate attributes; but enough of the original difference remains to show that our legislation not only carefully preserves the distinction of names, but sufficient, also, of the original difference of character and quality to disclose a clear intent not to merge the two. We may thus see upon what the legislative intent to preserve them as separate and distinct is founded, and what distinguishing characteristics remain. The formation of the one involves the merging and destruction of the common-law liability of the members for the debts, and requires the substitution of a new, or retention of the old, liability by an affirmative enactment which avoids the inherent effect of the corporate creation. In the other the common-law liability remains unchanged and unimpaired, and needing no statutory intervention to preserve or restore it. The debt of the corporation is its debt, and not that of its members. The debt of the joint-stock company is the debt of the associates, however enforced. The creation of the corporation merges and drowns the liabilities of its corporators. The creation of the stock company leaves unharmed and unchanged the liability of the associates. The one derives its existence from the contract of individuals; the other, from the sovereignty of the state. The two are alike, but not the same. More or less they crowd upon and overlap each other, but without losing their identity; and so, while we cannot say that the joint-stock company is a corporation, we can say, as we did say, in *Van Aernam v. Bleistein*, 102 N. Y. 360, 7 N. E. 537, that a joint-stock company is a partnership, with some of the powers of a corporation." See *Oliver v. Insurance Co.*, 100 Mass. 531; *Bray v. Farwell*, 81 N. Y. 600.

ficial person. It is therefore held to be a "person," within the meaning of statutes, using that term when the purpose and reason of the law include corporations as well as natural persons.⁶³ Thus, where a statute prohibited any "person" from engaging in the business of banking, except under certain circumstances, but did not expressly refer to corporations, it was held that they were included under the term "person."⁶⁴ The rule may be laid down that whenever a statute conferring a right or remedy, or imposing a duty or liability, upon "persons," applies in reason and design to corporations, but not otherwise, they are to be deemed included, though not specially mentioned.⁶⁵ The same is true of statutes using the word "inhabitant" or the word "occupier."⁶⁶ On the same principle, a corporation may be regarded as a "citizen," within the meaning of a statute using that term, though it does not expressly refer to corporations. The statute is to be construed as referring to them, if they are within its reason and design, but not otherwise. Thus, a corporation is to be deemed a "citizen," within the meaning of the acts of congress defining the jurisdiction of the federal courts.⁶⁷ But it is not a "citizen," within the meaning of the provision of the federal constitution that "the citizens of each state shall be entitled to all the privileges and immunities of citizens in the several states."⁶⁸

⁶³ Ang. & A. Corp. § 6.

⁶⁴ *People v. Utica Ins. Co.*, 15 Johns. (N. Y.) 358.

⁶⁵ *People v. Utica Ins. Co.*, supra; *Denny Hotel Co. v. Schram*, 6 Wash. 134, 32 Pac. 1002; *School Directors v. Carlisle Bank*, 8 Watts (Pa.) 289; *State v. President & Directors of Bank of Maryland*, 6 Gill & J. (Md.) 205; *Fisher v. Manufacturing Co.*, 10 Wis. 351; *Planters' & Merchants' Bank v. Andrews*, 8 Port. (Ala.) 404; *Mineral Point R. Co. v. Keep*, 22 Ill. 9; *Grand Gulf Bank v. Archer*, 8 Smedes & M. (Miss.) 151; *Baltimore & O. R. Co. v. Gallahue's Adm'r*, 12 Grat. (Va.) 655; *Proprietors of Jeffries Neck Pasture v. Inhabitants of Ipswich*, 158 Mass. 42, 26 N. E. 239. A corporation is not a person, within the meaning of the constitutional provision that no state shall deny to any "person" within its jurisdiction the equal protection of its laws. Post, p. 616.

⁶⁶ 2 Inst. 708; *Rex v. Gardner*, 1 Cowp. 79; *Gormully & Jeffrey Manuf'g Co. v. Pope Manuf'g Co.*, 34 Fed. 818; post, p. 637.

⁶⁷ Post, p. 74.

⁶⁸ *Ducat v. City of Chicago*, 48 Ill. 172; *Tatem v. Wright*, 23 N. J. Law, 429; post, p. 616.

KINDS OF CORPORATIONS.**10. Corporations may be classified as follows:**

- (a) According to their membership, they are sole or aggregate.**
 - (1) Corporations sole are composed of only one member at a time.**
 - (2) Corporations aggregate are composed of more than one member.**
- (b) According to their object, they are religious, eleemosynary, or civil.**
 - (1) Religious corporations are such as are created to carry out some religious object.**
 - (2) Eleemosynary corporations are such as are created to carry out some charitable object.**
 - (3) Civil corporations comprise all corporations other than those defined above, such as public corporations and private business corporations.**
- (c) Civil corporations are divided into public and private corporations. Religious and eleemosynary corporations are private.**
 - (1) Public corporations are such as are created for the purpose of government and the management of public affairs, like cities and villages, etc., and banks, hospitals, etc., founded by the state, and managed by it for governmental purposes.**
 - (2) Private corporations are such as are created for private purposes, as manufacturing, banking, and railroad corporations. Religious and eleemosynary corporations are also included.**
- (d) Civil corporations are again divided into stock and nonstock corporations.**

- (1) In stock corporations, membership, with its attendant rights, privileges, and liabilities, is determined solely by the ownership of stock.
- (2) In nonstock corporations, membership depends upon the consent and agreement of the associates.

11. Quasi corporations are bodies having some, but not all, of the powers and faculties of a corporation.

Sole and Aggregate Corporations.

A corporation sole consists of a single member only at one time. When he dies, or for any other reason ceases to be a member, there is some other person who takes his place, so that the corporation, though it may consist of only one natural person, has perpetual or continuous succession.⁶⁹ The sovereign of England has always been regarded as a corporation sole, because of the office, which is clothed with perpetuity. A bishop, dean, parson, and vicar are also given in the English books as instances of corporations sole, and they and their successors take the corporate property and privileges in succession.⁷⁰ In this country the governor of a state has been held a quasi sole corporation.⁷¹ There are also instances in the books of ministers of a parish, seised of parsonage lands in the right of the parish, being held to be corporations sole.⁷² For certain purposes, also, public officers have at times been expressly or impliedly created corporations sole by statute.⁷³ Unless authorized by stat-

⁶⁹ As to the distinction between corporations sole and aggregate, see *Overseers of Poor of City of Boston v. Sears*, 22 Pick. (Mass.) 122.

⁷⁰ 1 Bl. Comm. 469; 2 Kent, Comm. 273.

⁷¹ *Governor v. Allen*, 8 Humph. (Tenn.) 176. And see *State v. Woram*, 6 Hill (N. Y.) 33.

⁷² *Weston v. Hunt*, 2 Mass. 500; *Inhabitants of First Parish in Brunswick v. Dunning*, 7 Mass. 445; *Terrett v. Taylor*, 9 Cranch, 43, 46. Such a corporation exists at this day by statute in Kentucky, and perhaps in other states. See *McCloskey v. Doherty* (Ky.) 30 S. W. 649.

⁷³ Thus, when a statute directs bonds for the public benefit to be made payable to a public officer, the office is the real obligee, and the successor in office, whether described eo nomine in the statute or bond or not, may maintain an action on the bond, since the officer is quoad hoc a corporation sole. See *Polk v. Plummer*, 2 Humph. (Tenn.) 500, 37 Am. Dec. 566; *Jansen v. Ostrander*, 1 Cow. (N. W.) 670.

ute, a corporation sole cannot take personal property in succession, but their capacity in this respect is limited to real property.⁷⁴

In this country corporations sole are very rare. Almost all of our corporations are aggregate; that is, they consist of more than one member at a time.⁷⁵ Private civil corporations are all aggregate. The legislature would, doubtless, have the power to create a sole corporation for private business purposes; but it is perhaps safe to say that it will never do so. It may happen in a stock corporation that, by the purchase of all the stock, the membership may be reduced to one person; but this would not make it a corporation sole. The several shares would be treated as distinct, and liable to be again distributed by the sole owner.*

Religious, Eleemosynary, and Civil Corporations.

In English law, corporations are divided into ecclesiastical and lay. The former were those of which the members were spiritual persons, and the object of the institution was also spiritual.⁷⁶ In this country we have no strictly ecclesiastical corporations in the sense of the English law. But we have religious corporations. These are private civil corporations created for the purpose of holding property in succession for advancing the particular tenets and articles of faith which the corporation was organized to uphold and advance. They are mere trustees of the property, and cannot divert it to other purposes.⁷⁷

Lay corporations are divided into eleemosynary and civil corporations. Eleemosynary corporations are like religious corporations, except that the property is held in trust for certain designated charities. Their object is to provide for the perpetual distribution, or continuous distribution for a certain period, of the bounty of their

⁷⁴ 2 Kent, Comm. 273, 274.

⁷⁵ *Overseers of Poor of City of Boston v. Sears*, 22 Pick. (Mass.) 122.

* Post, p. 234.

⁷⁶ 2 Kent, Comm. 274.

⁷⁷ *Van Houten v. McKelway*, 17 N. J. Eq. 126; *Watson v. Jones*, 13 Wall. 679; *Robertson v. Bullions*, 11 N. Y. 243. See *Silsby v. Barlow*, 16 Gray (Mass.) 829. Where there is a division in a church, and part—even a majority—of the members secede, that portion of the church which remains in full connection with the body under which they were organized as a congregation continues the corporate existence, and is entitled to all the property and privileges of the corporation. *Baker v. Fales*, 16 Mass. 488; *Gable v. Miller*, 10 Paige (N. Y.) 627.

founders to such objects as they direct. Hospitals, asylums, colleges, and universities are examples of eleemosynary corporations.⁷⁸

All other corporations than religious and eleemosynary are called "civil." Indeed, with us, religious corporations are civil.

Public and Private Corporations.

By far the most important division of corporations is into public and private. It is of the latter class only that we are to treat. As between these two classes of corporations, there is a real divergence, both in the modes of operation, and in the principles of law which govern their acts, and their rights and obligations. Public corporations are such as are created for the purposes of government and the management of public affairs. Private corporations are those founded for the management of affairs in which the members are interested as private persons. Counties, cities, towns, and villages are examples of public corporations. These are also called municipal corporations.

A bank, a hospital, or other institution may be a public, as distinguished from a private, corporation, and therefore within the absolute control of the legislature. If a corporation is founded for a public purpose, and the entire interest therein belongs to the government, it is a public corporation; but not if there are any private owners of stock or shares therein. A bank created by the government for its own purposes, and whose stock or shares are owned exclusively by the government, would be a public corporation; but a bank whose stock is owned partly by private persons is a private corporation, although it is erected by the government, and its object and operations partake of a public nature.⁸⁰ So, also, a hospital, asy-

⁷⁸ Trustees of Dartmouth College v. Woodward, 4 Wheat. 517, 1 Cumming, Cas. Priv. Corp. 490, W. D. Smith, Cas. Corp. 148; Shep. Cas. Corp. 248; American Asylum v. President, Directors, etc., of Phoenix Bank, 4 Conn. 172; Trustees of Phillips Academy v. King, 12 Mass. 546; Board of Education v. Greenebaum, 39 Ill. 609; Board of Education v. Bakewell, 122 Ill. 339, 10 N. E. 878; Bakewell v. Board (Ill. Sup.) 83 N. E. 186.

⁸⁰ 2 Kent, Comm. 276; Per Story, J., in Trustees of Dartmouth College v. Woodward, 4 Wheat. 517, 669; Bank of U. S. v. Planters' Bank, 9 Wheat. 907; Miners' Bank v. U. S., 1 G. Greene (Iowa) 553, 561; Turnpike Co. v. Wallace, 8 Watts (Pa.) 816; Attorney General v. Simonton, 78 N. C. 57; President & Directors of State Bank v. Brown, 1 Scam. (Ill.) 106. Compare Bank of South

lum, college, university, or other charitable institution, created and endowed by the government alone for general charity, is a public corporation; but a hospital or asylum or institution of learning which is founded and endowed in whole or in part by private persons, though partly endowed by the government, is a private eleemosynary corporation, however general the charity may be.⁸¹ Insurance, canal, railroad, steamship, bridge, and turnpike companies, the shares in which are owned in whole or in part by private individuals, are private corporations, though their uses are public in their nature.⁸² These are sometimes called quasi public corporations. The trustees or commissioners of public schools and universities are public corporations or quasi corporations.⁸³

A corporation may be a public or quasi public body in respect to some of its functions and powers, and a private corporation in respect to others. Thus, it has been held that a municipal corporation, to which the legislature has given the power to erect water-

Carolina v. Gibbs, 3 McCord (S. C.) 377; *Bank of Alabama v. Gibson's Adm'rs*, 6 Ala. 814. See 1 Thomp. Corp. § 24. A bank is not a public corporation because the state holds stock in it, if any stock is held by private individuals. "When a government becomes a partner in a trading company, it divests itself, so far as concerns the transactions of that company, of its sovereign character, and takes that of a private citizen." *Bank of U. S. v. Planters' Bank*, *supra*.

⁸¹ *Trustees of Dartmouth College v. Woodward*, 4 Wheat. 518, 630, 667, 1 Cumming, Cas. Priv. Corp. 490, W. D. Smith, Cas. Corp. 148, Shep. Cas. Corp. 248; *Regents v. Williams*, 9 Gill & J. (Md.) 365; *Board of Education v. Greenebaum*, 39 Ill. 609; *Board of Education v. Bakewell*, 122 Ill. 339, 10 N. E. 878; *Head v. University of Missouri*, 47 Mo. 220; *Society for the Propagation of the Gospel v. Town of New Haven*, 8 Wheat. 464; *Board of Trustees for Vincennes University v. State*, 14 How. 268; *Downing v. Board*, 129 Ind. 443, 28 N. E. 123, 614. See 1 Thomp. Corp. §§ 25, 26.

⁸² *Tinsman v. Railroad Co.*, 26 N. J. Law, 148; *Rundle v. Delaware & R. Canal*, 1 Wall. Jr. 275, Fed. Cas. No. 12,139; *Bonaparte v. Railroad Co.*, Baldw. 205, Fed. Cas. No. 1,617; *Ten Eyck v. Canal Co.*, 18 N. J. Law, 200; *Board of Directors v. Houston*, 71 Ill. 318. See 1 Thomp. Corp. § 27. Contra, where a turnpike corporation consists solely of officers of the state, and is organized solely for the public benefit. *Sayre v. Turnpike Road*, 10 Leigh (Va.) 454.

⁸³ *Trustees of Schools v. Tatman*, 13 Ill. 27; *Bradley v. Case*, 3 Scam. (Ill.) 585; *Mobile School Com'rs v. Putnam*, 44 Ala. 506; *Head v. University of Missouri*, 47 Mo. 220; *Trustees of University v. Winston*, 5 Stew. & P. (Ala.) 17; 1 Thomp. Corp. § 25.

works, for the private advantage and emolument of the municipality, is to be regarded quoad hoc a private corporation, and responsible, as such, for injuries inflicted in the management of the works.⁸⁴

Stock and Nonstock Corporations.

Private corporations are also divided into stock and nonstock corporations. In the former the membership, after incorporation, with its attendant rights, privileges, and liabilities, is determined by the ownership of stock. Any stockholder may transfer his stock, and the transferee will become a member, without regard to the consent of the other stockholders. This is the most common kind of private business corporations. In nonstock corporations there are no shares of stock to be transferred. Membership depends upon the consent of the associates. Incorporated mutual benefit associations are examples of this kind of private corporations.

Quasi Corporations.

A quasi corporation is a body which has some, but not all, of the powers of a corporation. Towns, counties, and school districts, etc., are not strictly public corporations, but they have some of the pow-

⁸⁴ *Bailey v. Mayor, etc.*, 3 Hill (N. Y.) 531. In this case it was said that, if powers are granted to a municipal corporation for public purposes exclusively, they belong to the corporate body in its public, political, or municipal character; "but if the grant is for purposes of private advantage and emolument, though the public may derive a common benefit therefrom, the corporation, quoad hoc, is to be regarded as a private company." See, also, *De Voss v. City of Richmond*, 18 Grat. (Va.) 838; *Macauley v. Mayor, etc.*, 67 N. Y. 602; *Oliver v. City of Worcester*, 102 Mass. 489, 499; *City of Memphis v. Kimbrough*, 12 Heisk. (Tenn.) 133; *People v. Hurlbut*, 24 Mich. 44; *County of Richland v. County of Lawrence*, 12 Ill. 8. Compare *Mead v. City of New Haven*, 40 Conn. 72; *Eastman v. Meredith*, 36 N. H. 284. In *De Voss v. City of Richmond*, supra, it was held that a municipal corporation, in exercising the power to borrow money and to issue bonds therefor, is not acting in its public capacity, but merely as a private corporation, and that it is therefore responsible as such for the act or default of its agent. And in *Oliver v. City of Worcester*, supra, a municipal corporation was held liable for injuries to a person from falling into an excavation on the grounds of a building which was only partly used for public purposes, the other part being rented to private individuals. Contra, where the building is used wholly for public purposes. *Eastman v. Meredith*, supra. And see *Hill v. City of Boston*, 122 Mass. 351; *Stilling v. Town of Thorp*, 54 Wis. 532, 11 N. W. 906; *City of Chicago v. Turner*, 80 Ill. 423; *Symonds v. Board*, 71 Ill. 357; *Moulton v. Inhabitants*, 71 Me. 269.

ers of a corporation, as the faculty of succession, the power to sue and be sued as a body, etc. For this reason they are called quasi corporations.⁸⁵ Other quasi corporations are overseers of the poor, county commissioners, and other public boards or officers.⁸⁶

⁸⁵ Ang. & A. Corp. §§ 23, 24; *Riddle v. Proprietors*, 7 Mass. 187; *Town of North Hempstead v. Town of Hempstead*, 2 Wend. (N. Y.) 109; *Inhabitants of Fourth School Dist. v. Wood*, 13 Mass. 199; *Board of Com'rs of Hamilton Co. v. Mighels*, 7 Ohio St. 109; *Andrews v. Estes*, 11 Me. 267; *McLoud v. Selby*, 10 Conn. 390; *Gaskill v. Dudley*, 6 Metc. (Mass.) 546; *Boone, Corp.* § 10; note in 18 Am. Dec. 523.

⁸⁶ *Polk v. Plummer*, 2 Humph. (Tenn.) 500; *Overseers of the Poor v. Sears*, 22 Pick. (Mass.) 122; *Governor v. Allen*, 8 Humph. (Tenn.) 176; *Levy Court v. Coroner*, 2 Wall. 501; *Todd v. Birdsall*, 1 Cow. (N. Y.) 260; *Van Kirk v. Clark*, 16 Serg. & R. (Pa.) 286.

CHAPTER II.

CREATION AND CITIZENSHIP OF CORPORATIONS.

- 12. Creation—In General.**
- 13-18. Power to Create.**
 - 14. State Legislatures.**
 - 15. Congress.**
 - 16. Territorial Legislatures.**
 - 17. Prescription.**
 - 18. Delegation of Power.**
- 19-20. General and Special Laws.**
 - 21. Ratification of Claim to Corporate Existence.**
 - 22. Intention to Create.**
- 23-24. Agreement between Corporation and State—Acceptance of Charter.**
 - 25. Place of Organization.**
 - 26. Compliance with Conditions Precedent.**
 - 27. Agreement between Corporators and Corporation.**
- 28-29. Who may Become Corporators.**
- 30-31. Purpose of Incorporation.**
- 32-35. Corporate Name.**
- 36-38. Residence and Citizenship of Corporations.**
 - 39. Extension of Charter—Creation of New Corporation.**
 - 40. Proof of Corporate Existence.**

CREATION—IN GENERAL.

- 12. To the creation or formation of a corporation, the following things are essential:**
- (a) A grant of authority, or charter, from the state.**
 - (b) Acceptance of the grant, or an agreement between the state and the corporators.**
 - (c) An agreement between the corporators and the corporation.**

POWER TO CREATE CORPORATIONS.

- 13. It is essential to the existence of a corporation that it shall have been created or authorized by the state.**

Mere agreement between the members, as in the

case of a partnership, is not enough. In this country such bodies can be created only by or under legislative enactment.

14. **STATE LEGISLATURES**—The state legislatures have absolute and unlimited power to create corporations, except in so far as they may be controlled by restrictions in the state or federal constitution.
15. **CONGRESS**—Congress, acting as the legislature of the United States, has the power to create a corporation, if its existence is an appropriate means of carrying into effect any of the powers conferred upon the United States government by the federal constitution. As the local legislature of the District of Columbia, it has the same power in the District as the state legislatures have in the states, subject only to the restrictions of the federal constitution.
16. **TERRITORIAL LEGISLATURES**—Territorial legislatures, vested with general legislative powers, have the power to create corporations, which will not be affected by the admission of the territory into the Union, and the adoption of a state constitution.
17. **PRESCRIPTION**—Long-continued use of corporate powers, and acquiescence on the part of the public, may raise a presumption of legislative authority in the case of public, and, it seems, even in the case of private, corporations. These are corporations by prescription.
18. **DELEGATION OF POWER**—The legislature cannot delegate its power to create corporations, but, in providing for the formation of a corporation, it may allow ministerial acts to be performed by courts or officers.

Individuals, under their right to make contracts and acquire property, have an absolute right to form partnerships, including

joint-stock companies, for the purpose of carrying on any lawful business. For this purpose no authority from the state is necessary. But they have no such right to form a corporation, and conduct their business in that privileged mode, by a mere agreement between themselves. A corporation can only be created by the state,—with us, by or under legislative authority.¹ Special authority seems not to have been necessary at one time under the Roman law, but later it was required even under that law;² and authority from the sovereign or state has always been necessary at common law. Lord Coke, in enumerating the things essential to a corporation, states the first to be “Lawful authority of incorporation,” and he says that this may be “by four means,—sc., by the common law, by the king himself, by authority of parliament, by the king’s charter, and by prescription.”³ In England, the king, bishops, parsons, etc., were corporations by the common law. In this country there are no common-law corporations. All corporations, both public and private, are the creatures of the legislature. There are a few corporations in this country which were chartered by the English crown or by parliament before the Revolution, under the colony administration, and whose charters are still recognized.⁴

Corporations by Prescription.

In England, both public and private corporations may exist by prescription; that is, they may have existed for so long a time that the king’s consent will be presumed. Blackstone, after mentioning the king, bishops, and other common-law corporations sole, says: “Another method of implication, whereby the king’s consent is presumed, is as to all corporations by prescription, such as the city of London, and many others, which have existed as corporations, time whereof the memory of man runneth not to the contrary, and therefore are looked upon in law to be well created; for though the members thereof can show no legal charter of incorporation, yet in cases

¹ *Stowe v. Flagg*, 72 Ill. 397; *Medical Inst. v. Patterson*, 1 Denio (N. Y.) 61; *Myers v. Manhattan Bank*, 20 Ohio, 283; *McKim v. Odom*, 3 Bland, Ch. (Md.) 407, 416; *Ang. & A. Corp.* § 66 et seq.

² *Tayl. Corp.* § 4; 1 *Wat. Corp.* § 22.

³ *Sutton’s Hospital Case*, 10 Coke, 29b, 2 *Cumming, Cas. Priv. Corp.* 14.

⁴ *Trustees of Dartmouth College v. Woodward*, 4 Wheat. 517, 1 *Cumming, Cas. Priv. Corp.* 490, *W. D. Smith, Cas. Corp.* 148, *Shep. Cas. Corp.* 248.

of such high antiquity the law presumes there once was one, and that, by the variety of accidents which a length of time may produce, the charter is lost or destroyed." * The same doctrine has frequently been applied in this country in the case of public corporations.⁶ There seems to be no good reason for recognizing any distinction in this respect between public and private corporations, for both are the creatures of the legislature; and the doctrine has been applied to private corporations also.⁷ To give rise to this presumption, the acts done must bear the impress of corporate acts; that is, they must be such as corporations are competent, and individuals incompetent, to perform.⁸

Power of the State Legislatures.

The power of the state legislatures to create corporations, and confer powers and privileges upon them, within the state, is absolute, except in so far as it may be restricted by the state or federal constitution.⁹ In the absence of constitutional limitations, there is nothing to prevent the legislature from creating a corporation, and conferring exclusive privileges upon it, in consideration of public services, though it may thus create a monopoly.¹⁰

* 1 Bl. Comm. 473.

⁶ "Municipal corporations," said the Illinois court, "are created for the public good,—are demanded by the wants of the community; and the law, after long-continued use of corporate powers, and the public acquiescence, will indulge in presumptions in favor of their legal existence." *Jameson v. People*, 16 Ill. 257. And see *People v. Maynard*, 15 Mich. 463, 470; *Bow v. Allentown*, 34 N. H. 351; *Dillingham v. Snow*, 5 Mass. 547.

⁷ 2 Kent, Comm. 276, 277; *Greene v. Dennis*, 6 Conn. 293.

⁸ *Greene v. Dennis*, *supra*.

⁹ *People v. Marshall*, 6 Ill. 672; *Bell v. Bank of Nashville*, Peck (Tenn.) 269. See *Myers v. Manhattan Bank*, 20 Ohio, 283.

¹⁰ *Thomp. Corp.* §§ 647–650. See *State v. Milwaukee Gaslight Co.*, 29 Wis. 454; *Louisville Gas Co. v. Citizens' Gaslight Co.*, 115 U. S. 683, 6 Sup. Ct. 265; *New Orleans Gaslight Co. v. Louisiana Light & H. P. & Manuf'g Co.*, 115 U. S. 650, 6 Sup. Ct. 252. Contra, *Norwich Gaslight Co. v. Norwich City Gas Co.*, 25 Conn. 20. Thus, the legislature may, in the absence of constitutional restrictions, grant a corporation the exclusive privilege of maintaining a railroad in the street. *Case of Philadelphia & T. R. Co.*, 6 Whart. (Pa.) 25. And it may grant a corporation the exclusive privilege of manufacturing and selling illuminating gas in a city, and of constructing works and laying pipes for such purpose. *State v. Milwaukee Gaslight Co.*, *supra*; *Louisville Gas Co. v. Citizens'*

In all of the state constitutions some limitations on the power of the legislature to create corporations, and grant privileges to them, will be found. In some states, for instance, it is declared that no act of incorporation shall be passed unless with the assent of two-thirds of each house.¹¹ And in most states, as we shall presently see at some length, the legislature is prohibited from creating corporations, with some exceptions, by special act, but must provide for their formation, if at all, by general laws.¹² In most states there is a constitutional provision that no bill passed by the legislature shall contain more than one subject, and that this subject shall be clearly expressed in its title. This applies, of course, to acts in relation to corporations.¹³ The only restrictions upon the power of the several

Gaslight Co., *supra*; New Orleans Gaslight Co. v. Louisiana Light & H. P. & Manuf'g Co., *supra*. Contra, Norwich Gaslight Co. v. Norwich City Gas Co., *supra*. And it may grant the exclusive privilege of supplying a city with water, and of constructing works and laying pipes for that purpose. New Orleans Waterworks Co. v. Rivers, 115 U. S. 674, 6 Sup. Ct. 273. In most states, perhaps, there are constitutional provisions prohibiting the legislature from granting exclusive privileges to any man or set of men, except in consideration of public services. Such a provision would not prevent the granting of exclusive privileges, like those referred to above, to water and gas companies, for the services in such cases are public. The legislature, however, could not grant exclusive privileges in matters not of such character. It could not, for instance, allow a corporation to charge a greater rate of interest than is allowed by the general law. *Gordon v. Association*, 12 Bush (Ky.) 110.

¹¹ See, as to this provision, 1 *Thomp. Corp.* §§ 632-636. Some of the courts have held that this provision is aimed at special acts only, and that it does not prohibit the passing of general incorporation laws by a mere majority vote. *Gifford v. Livingston*, 2 Denio (N. Y.) 880; *Palmer v. Lawrence*, 5 N. Y. 889. Others have held that it covers all laws for the creation of corporations, general as well as special. *Falconer v. Campbell*, 2 McLean, 195, Fed. Cas. No. 4,620; *Green v. Graves*, 1 Doug. (Mich.) 361. It has been held that this provision does not prevent the legislature from creating more than one corporation by the same act, provided the act is passed by the necessary two-thirds majority; and that, therefore, it does not prevent the legislature from passing general laws for the formation of corporations. *Falconer v. Campbell*, *supra*; *Thomas v. Dakin*, 22 Wend. (N. Y.) 9.

¹² *Post*, p. 42.

¹³ As to this provision, see 1 *Thomp. Corp.* §§ 607-627. See, also, *State v. Illinois Cent. R. Co.*, 88 Fed. 780, 765; *People v. Mahaney*, 18 Mich. 481; *Astor v. New York Arcade Ry. Co.*, 118 N. Y. 93, 20 N. E. 594. The provision must receive "a fair and reasonable construction,—one which will repress the evil de-

states, in the creation of corporations, that are to be found in the federal constitution, relate to the purposes for which corporations

signed to be guarded against, but which at the same time will not render it oppressive or impracticable." *Belleville & I. R. Co. v. Gregory*, 15 Ill. 20. This provision does not prohibit an act of incorporation from granting various powers; nor does it require all the powers granted to be enumerated in the title. 1 *Thomp. Corp.* § 618. See *Lockhart v. City of Troy*, 48 Ala. 579; *Montgomery Mut. Bldg. & Loan Ass'n v. Robinson*, 69 Ala. 413. While the subject must be expressed in the title, "the adjuncts to that subject, or the *modus operandi*, need not be." *City of Ottawa v. People*, 48 Ill. 233. The constitution "does not require that the subject of the bill must be specifically and exactly expressed in the title; hence we conclude that any expression in the title which calls attention to the subject of a bill, although in general terms, is all that is required." *Johnson v. People*, 83 Ill. 431. In *Mississippi & R. R. Boom Co. v. Prince*, 84 Minn. 79, 24 N. W. 861, an act entitled "An act relating to the Mississippi Boom Corporation," which, in addition to provisions relating to the powers and duties of that corporation, embraced a separate section imposing additional duties upon another corporation, was held void as to such section because the subject-matter thereof was not embraced in the title of the act. And in *Eaton v. Walker*, 76 Mich. 579, 43 N. W. 638, an act amending an act for the incorporation of manufacturing companies, so as to include corporations for mercantile business, the title of the amended act being "An act for the incorporation of manufacturing companies," and being unchanged, was held void. This clause of the constitution is "construed liberally in favor of the validity of enactments; and the fact that many things of a diverse nature are authorized or required to be done is unimportant, provided the doing of them may fairly be regarded as in furtherance of the general subject of the enactment." *Blake v. People*, 109 Ill. 504. The following acts have been sustained as embracing only one subject, which was embraced in its title: "An act to incorporate the Firemen's Benevolent Association, and for other purposes," which contained a provision requiring the agents of all foreign insurance companies doing business in Chicago to pay to the association a certain per cent. of all premiums received by them. *Firemen's Benevolent Ass'n v. Lounsbury*, 21 Ill. 511. "An act to amend an act entitled 'An act to incorporate the Northwestern University,'" which contained a prohibition against the sale of intoxicating liquors within a certain distance of the university. *O'Leary v. County of Cook*, 28 Ill. 534. An act providing for the incorporation of mutual fire insurance companies, and repealing certain existing acts, which, in the absence of such express repeal, would be repealed by implication. *Telford v. Church*, 66 Mich. 431, 33 N. W. 913. "An act to authorize the organization of annuity, safe-deposit and trust companies," granting to such corporations power to act as guardian, etc. The latter section of the act, said the court, "is but an enumeration of the powers granted to such corporations, and it was never before heard that, in a general law for the organization of a particular class of corporations, the powers granted to them should be detailed in

may be formed. No state can create a corporation for a purpose that is expressly or impliedly prohibited by that instrument.¹⁴

Power of Congress and of Territorial Legislatures.

The congress of the United States derives all its powers from the federal constitution, but it is not limited to the powers expressly conferred upon it by that instrument. There is a general clause giving it the power to pass all necessary and proper laws for carrying its powers into execution. Indeed, it has such power independently of this clause, for a grant of power necessarily implies the grant of all usual and proper means for its execution. It is under this general clause, or the implied grant of power, that congress has the power to establish corporations. The power is nowhere expressly conferred. Congress, then, has the power, acting as the legislative body of the federal government, to create a corporation, when its existence is necessary or proper to enable the federal government to execute the powers expressly or impliedly conferred upon it by the constitution. It can create a corporation as a means, but not as an end.¹⁵ If the creation of a corporation is an appropriate means to

the title of the act." *Minnesota Loan & Trust Co. v. Beebe*, 40 Minn. 7, 41 N. W. 232. In *Wardle v. Townsend*, 75 Mich. 385, 42 N. W. 950, it was held that the title, "An act to provide for the incorporation of mutual fire insurance companies, and defining their powers and duties," was sufficient to embrace provisions for winding up such companies when insolvent, for their examination by the insurance commissioner, the appointment of a receiver, and the assessment of policy holders to pay liabilities. The following acts have been held void as embracing more than one subject: An act incorporating, or reviving the charters of, several distinct corporations. *Ex parte Conner*, 51 Ga. 571. *Contra*, *People v. Ottawa Hydraulic Co.*, 115 Ill. 281, 3 N. E. 413. "An act to provide for the incorporation of merchants' mutual insurance companies, and to regulate the business of insurance by merchants' and manufacturers' mutual insurance companies." *Skinner v. Wilhelm*, 63 Mich. 568, 30 N. W. 311. By the weight of authority, an act incorporating a railroad company may also provide for municipal aid. 1 *Thomp. Corp.* § 614; *Phillips v. Bridge Co.*, 2 Metc. (Ky.) 219; *Phillips v. Town of Albany*, 28 Wis. 340; *Mahomet v. Quackenbush*, 117 U. S. 508, 6 Sup. Ct. 858. *Contra*, *People v. Hamill*, 134 Ill. 666, 17 N. E. 799 (but see *Board of Super's v. People*, 25 Ill. 182); *Peck v. City of San Antonio*, 51 Tex. 490.

¹⁴ 1 *Mor. Priv. Corp.* § 14.

¹⁵ *McCulloch v. State of Maryland*, 4 Wheat. 316. See, as to national corporations, 1 *Thomp. Corp.* §§ 665-683. Under this implied grant of power, congress has created a United States banking corporation. *McCulloch v. State of Maryland*,

carry into effect any of the powers conferred upon the federal government by the constitution, the degree of its necessity is a question within the discretion of congress, and not a question of judicial cognizance.¹⁶

Congress also has the power to create corporations in the District of Columbia, and it has the same power in this respect as the state legislature has in a state, subject only to the restrictions of the federal constitution.¹⁷ In the exercise of this power, however, it acts, not as the legislature of the United States, but as the local legislature of the District.¹⁸

It has been held that territorial legislatures have the power to create corporations under the general legislative powers conferred upon them by congress in the organic act; and a corporation created by a territorial legislature is not in any way affected by the admission of the territory into the Union, and the adoption of a state constitution.¹⁹ Territorial legislatures are now expressly authorized to provide for the formation of corporations by general laws, but prohibited from granting private charters or special privileges.²⁰

A corporation created by the government of the United States is a creature of federal sovereignty alone, and is controllable by, and amenable to, the federal government only.²¹

Delegation of Power by the Legislature.

It was formerly asserted in England that the act of incorporation must be the immediate act of the king himself, and that he could not *supra*; *Osborn v. Bank of U. S.*, 9 Wheat. 738. And see *State v. Curtis*, 35 Conn. 374. So, under the power to regulate commerce, it has created corporations with power to construct railways and highways across the various states and territories, and corporations to construct bridges across navigable rivers. *Union Pac. R. Co. v. Lincoln Co.*, 1 Dill. 314, Fed. Cas. No. 14,378; *Thomson v. Pacific R. R.*, 9 Wall. 579; *California v. Central Pac. R. Co.*, 127 U. S. 1, 8 Sup. Ct. 1073; *Indiana v. United States*, 148 U. S. 148, 13 Sup. Ct. 564; *Luxton v. North River Bridge Co.*, 153 U. S. 525, 14 Sup. Ct. 891.

¹⁶ *McCulloch v. State of Maryland*, *supra*.

¹⁷ 1 *Thomp. Corp.* § 682; *Hadley v. Freedman's Savings & Trust Co.*, 2 *Tenn. Ch.* 122.

¹⁸ *Id.*

¹⁹ *Vincennes University v. State of Indiana*, 14 *How.* 268, 273; *Kansas Pac. Ry. Co. v. Atchison, T. & S. F. R. Co.*, 112 U. S. 414, 5 Sup. Ct. 208; 1 *Thomp. Corp.* § 681.

²⁰ *Rev. St. U. S.* § 1889.

²¹ *State v. Curtis*, 35 *Conn.* 374.

grant a license to another to create a corporation.²² But the law has since been settled to the contrary, and it is now held that the king may not only grant a license to a subject to create a particular corporation, but may give a general power by charter to erect corporations indefinitely on the principle, "Qui facit per alium facit per se;" the person to whom the power is delegated being regarded merely as an instrument in the hands of the government.²³ In this country our federal and state constitutions vest the lawmaking power exclusively in the federal and state legislatures, and the English rule does not obtain. With us, corporations are created by the legislatures, and not otherwise. To establish a corporate body is to enact a law, and no power but the legislature can do this. The maxim, "Delegata potestas non potest delegari," applies.²⁴

This principle does not prevent the legislature from delegating the performance of purely ministerial acts in the formation of corporations. Thus, it may enact a general law authorizing persons to form themselves into a corporation by complying with certain formalities, as by filing in a certain court of record, or with the secretary of state or some other officer, a petition setting forth the objects of the proposed corporation, and other facts, and providing for the making of an order by the court directing the petition to be entered of record, or the issuance of a certificate by the secretary or other officer, showing that the statute has been complied with, and declaring that the persons thus seeking to incorporate shall thereupon become a corporation, etc. A corporation thus formed is really created by the legislature, and not in any sense by the court or officer upon whom the ministerial duties are imposed. No discretionary power is conferred upon them. They are merely required to perform ministerial acts, and a writ of mandamus would lie to compel them to do so.²⁵

²² Case of Sutton's Hospital, 10 Coke, 27.

²³ Franklin Bridge Co. v. Wood, 14 Ga. 80, 1 Cumming, Cas. Priv. Corp. 42; Ang. & A. Corp. 74; 1 Kyd, Corp. 50; 1 Bl. Comm. 474.

²⁴ 1 Thomp. Corp. §§ 643-646; State v. Simons, 32 Minn. 540, 21 N. W. 750.

²⁵ Franklin Bridge Co. v. Wood, 14 Ga. 80, 1 Cumming, Cas. Priv. Corp. 42; In re New York El. R. Co., 70 N. Y. 327; Heck v. McEwen, 12 Lea (Tenn.) 97. In Granby Mining & Smelting Co. v. Richards, 95 Mo. 106, 8 S. W. 246, it was held that, where the powers of a corporation, and the procedure by which it can be brought into existence, are prescribed by the legislature, the fact that the

GENERAL AND SPECIAL LAWS.

19. In the absence of constitutional limitations, corporations may be created under or by either a general or a special law. In most states, however, the legislature is prohibited by the constitution from creating corporations, with certain exceptions, otherwise than under general laws.
20. By the weight of authority, such a provision does not prohibit a special act which merely grants additional powers and privileges to an existing corporation, but it does prohibit a special act so amending the charter of an existing corporation as to make it in effect a different corporation.

Corporations are created either by a special act of the legislature or under a general law. A special act creates a particular corporation. A general law does not of itself directly create a corporation, but authorizes incorporation by providing that any persons who comply with its terms shall thereby become incorporated. A general law authorizing the formation of corporations defines the purposes for which they may be formed, and prescribes the steps that must be taken to form them. It generally requires articles of association to be executed by the incorporators, and filed in some public office or court, and often fixes the minimum number of residents of the state who shall execute such articles. The articles are usually required to set forth the names of the incorporators and their residences, the name by which the proposed corporation shall be known, and its principal place of business, the object and purpose of the association, which, of course, must not be other than is authorized by the law under which it is formed,²⁶ the period of time for which

legislature, in the same act, gives such corporation the power to dispose of special stock which is to form no part of the general stock of the corporations, and permits the holders of such special stock to become a distinct corporation, is not such a delegation of legislative power as to render an organization formed under the special stock clause invalid.

²⁶ Post, p. 67.

the corporation is to exist, the number of directors, and the names of those who are to act as such until an election is had pursuant to the articles. If the body is to be a stock corporation, it is usually required that the articles shall state the amount of the capital stock, the number of shares, and the amount that is to be paid in before doing business. Of course, the requirements will vary greatly in the different states, and in different statutes in the same state.²⁷ As will presently be shown, the requirements of the statute must be complied with in order to form a legal corporation.²⁸

Constitutional Restriction.

In most states there is a constitutional provision that corporations, generally with some exceptions, shall not be created or formed by special act, but must be formed under general laws.²⁹ Where there is such a provision as this, the legislature, of course, has no power to create corporations, other than of the kind excepted, by a special act. The object of this provision is obvious. It is chiefly to prevent the granting of special privileges to one body of men, without giving all others the right to obtain them on the same conditions; and perhaps it is partly to prevent bribery and corruption of legislators.

²⁷ The following sections taken from a New Hampshire statute (Gen. Laws 1878, c. 152) are a good illustration of a general law:

"Section 1. Any five or more persons of lawful age may, by written articles of agreement, associate together for agricultural, educational, or charitable purposes, or for carrying on any lawful business, except banking and the construction and maintenance of a railroad; and when such articles have been executed and recorded in the office of the clerk of the town in which the principal business is to be carried on, and in that of the secretary of state, they shall be a corporation, and such corporation, its officers and stockholders, shall have all the rights and powers, and be subject to all the duties and liabilities of similar corporations, their officers and stockholders, except so far as the same are limited or enlarged by this chapter.

"Sec. 2. The object for which the corporation is established, the place in which its business is to be carried on, and the amount of capital stock to be paid in, shall be distinctly set forth in its articles of agreement."

²⁸ Post, p. 55.

²⁹ See Const. N. Y. art. 8, § 1; Const. Ill. art. 11, § 1; Const. Mich. art. 15, § 1; Const. Ind. art. 11, § 18; Const. Wis. art. 11, § 1; Const. Minn. art. 10, § 2; Const. Tenn. art. 11, § 8; Const. Tex. art. 12, § 1; Const. Mo. art. 12, § 2.

Where the provision of the constitution is that corporations "shall not be created" or "formed" by special act, it prevents the formation of a corporation by the acceptance after the adoption of the constitution of a special act offering a charter passed before its adoption, for "the restraint is plainly imposed upon the creation—the organization—of the corporation itself."⁸⁰ It is otherwise where the provision is that the legislature shall "pass no special act conferring corporate powers," for here the restraint is only imposed on future legislative action.⁸¹

The question has often arisen whether a constitutional prohibition against the creation or formation of a corporation by special act prohibits the legislature from passing a special act conferring additional privileges or powers upon a corporation previously created, or amending the charter of an existing corporation. It is sufficiently clear on principle, and has frequently been decided, that, where a corporation has already been created, a special act regulating it, or conferring new and additional grants, privileges, or powers, without changing the organization of the corporate body, is not within the prohibition.⁸² It has been held, for instance, that the constitution does not prohibit a special act conferring upon an existing railroad corporation authority to change the line of its road,⁸³ or to purchase the railroad and franchises of another company;⁸⁴ nor a special act extending the duration of an existing corporation,⁸⁵ or changing, or authorizing it to change, its name;⁸⁶ nor a special act changing the character of an existing corporation, as from a mutual benefit or nonstock corporation to a stock corporation.⁸⁷ As was said by Judge Sawyer:

⁸⁰ *State v. Dawson*, 16 Ind. 40, 1 Cumming, Cas. Priv. Corp. 65, W. D. Smith, Cas. Corp. 19, Shep. Cas. Corp. 54; *Snyder v. Studebaker*, 19 Ind. 462.

⁸¹ *State v. Roosa*, 11 Ohio St. 16; *State v. Dawson*, *supra*.

⁸² *Attorney General v. North America Life Ins. Co.*, 82 N. Y. 172.

⁸³ *Southern Pac. R. Co. v. Orton*, 32 Fed. 457.

⁸⁴ *Wallace v. Loomis*, 97 U. S. 146.

⁸⁵ *Cotton v. Boom Co.*, 22 Minn. 372. Compare *Logan v. Railroad Co.*, 87 Ga. 533, 13 S. E. 516.

⁸⁶ *Wallace v. Loomis*, 97 U. S. 146; *Hazelett v. Butler University*, 84 Ind. 230; *Attorney General v. Joy*, 55 Mich. 94, 20 N. W. 806. And see *Pacific Bank v. De Ro*, 37 Cal. 538; *Rosenthal v. Madison & I. P. Co.*, 10 Ind. 358.

⁸⁷ *St. Paul Fire & Marine Ins. Co. v. Allis*, 24 Minn. 75.

"The word 'create' has a clear, well-settled, and well-understood signification. It means to bring into being; to cause to exist; to produce; to make, etc. To my apprehension, it appears to be one thing to create, or bring into being, a corporation, and quite another to deal with it as an existing entity—a person—after it is created, by regulating its intercourse, relations, and acts as to other existing persons, natural and artificial."⁸⁸

The legislature, however, cannot resort to any subterfuge to avoid the constitutional prohibition. If by a special act it undertakes to so amend or alter the charter of an existing corporation as in effect to create a new corporate body, it violates the constitution, and the act is void. "A prohibition from creating corporations by special act undoubtedly does not, in terms, prohibit the legislature from passing a special law altering the charter of an existing corporation; but it is plain that a constitutional provision cannot be avoided, and practically annulled, by a subterfuge. A special law altering the character of an existing corporation, and practically changing it, must therefore be deemed in violation of a constitutional prohibition against the creation of corporations by special act. If this were not so, organizations formed under the general laws might be treated merely as the rough material out of which corporations might afterwards be fashioned at pleasure under special acts of the legislature, and the constitutional provision would become an empty form."⁸⁹

Some of the cases do not recognize this distinction, but hold broadly that the constitution prohibits a special act granting an existing corporation any new franchises,—“that there is no distinction, as respects the constitutional inhibition, between a grant of corporate

⁸⁸ In *Southern Pac. R. Co. v. Orton*, *supra*. See, also, *Wallace v. Loomis*, 97 U. S. 154; *Attorney General v. North America Life Ins. Co.*, 82 N. Y. 172; *In re New York El. R. Co.*, 70 N. Y. 327; *St. Joseph & L. R. Co. v. Shambaugh*, 106 Mo. 557, 17 S. W. 581; *State v. Cape Girardeau & S. L. R. Co.*, 48 Mo. 468.

⁸⁹ 1 *Mor. Priv. Corp.* § 12. For cases in which special acts in reference to existing corporations have been held void, see *Ex parte Pritz*, 9 Iowa, 30; *Town of McGregor v. Baylies*, 19 Iowa, 43; *City and County of San Francisco v. Spring Valley Waterworks*, 48 Cal. 493, overruling *California State Tel. Co. v. Alta Tel. Co.*, 22 Cal. 398 (but see the criticism of this case in *Southern Pac. R. Co. v. Orton*, 32 Fed. 457, 457); *Green v. Knife Falls Boom Corp.*, 35 Minn. 155, 27 N. W. 924; *Astor v. Railway Co.*, 113 N. Y. 93, 20 N. E. 594.

powers and privileges and the grant of corporate charters *de novo*.”⁴⁰

A special act waiving a failure to comply with conditions precedent in the attempted organization of a particular corporation under a general law is not unconstitutional under this clause;⁴¹ but it is otherwise if the legislature, by special act, attempts to ratify a claim to corporate existence which is altogether unauthorized.⁴²

In some states the language of the constitution is different from the provision we have been discussing; the legislature being prohibited from passing any special act “conferring corporate powers,” or “granting corporate powers or privileges.” Some of the courts regard this as broader than the prohibition against the “creation” of corporations, and have held that the legislature is thereby prohibited “from either creating corporations, or conferring upon the same corporate powers,” by special act.⁴³ This would seem to be the reasonable construction, but the weight of opinion seems to be against it, and in favor of holding such provisions merely equivalent to the prohibition against their “creation.”⁴⁴

An act is not “special,” within the meaning of the constitutions, if it operates alike and uniformly throughout the state upon like facts. An act, to be general, need not apply to every person or every corporation in the state. It is sufficient if it applies to every person or corporation who or which comes within the relations or circumstances provided for,⁴⁵ if the classification “has some reason-

⁴⁰ See *Green v. Knife Falls Boom Corp.*, *supra*; *City and County of San Francisco v. Spring Valley Waterworks*, *supra*; *Attorney General v. Chicago & N. W. R. Co.*, 35 Wis. 560.

⁴¹ *Central Agr. & Mech. Ass'n v. Insurance Co.*, 70 Ala. 120; *State v. Webb* (Ala.) 20 South. 462; *McAuley v. Railway Co.*, 83 Ill. 348; *Syracuse City Bank v. Davis*, 16 Barb. (N. Y.) 188.

⁴² *Oroville & V. R. Co. v. Supervisors of Plumas County*, 37 Cal. 354.

⁴³ *Atkinson v. Railroad Co.*, 15 Ohio St. 21. And see *German-American Inv. Co. v. City of Youngstown*, 68 Fed. 452. That such a clause prohibits a special act conferring upon an existing corporation the power to issue bonds, see *School Dist. v. Insurance Co.*, 103 U. S. 707.

⁴⁴ *Attorney General v. Chicago & N. W. R. Co.*, 35 Wis. 425; *Brady v. Moulton*, 61 Minn. 185, 63 N. W. 489; *North River Boom Co. v. Smith* (Wash.) 45 Pac. 750.

⁴⁵ 1 *Thomp. Corp.* §§ 592-602; *Hazelett v. University*, 84 Ind. 230; *Attorney General v. McArthur*, 38 Mich. 204; *Minnesota Loan & Trust Co. v. Beebe*, 40 Minn. 7, 41 N. W. 232; *Delaware Bay & C. M. R. Co. v. Markley* (N. J. Err. &

able foundation in the nature of things, and is not arbitrarily made to afford means of evading the constitutional inhibition."⁴⁶ The fact that the legislature expressly declares a special act to be general cannot make it so. If it were held otherwise, it would be an easy matter to defeat the constitutional inhibition.⁴⁷

In some states, special laws relating to corporations are prohibited only where general laws can be made applicable. Under such a provision, though there are some decisions to the contrary, it has generally been held that it is exclusively for the legislature, and not for the courts, to say whether a special law is necessary.⁴⁸

App.) 16 Atl. 436. In *Attorney General v. McArthur*, supra, it was held that the constitutional limitation upon the creation of corporations except by general laws does not apply to incorporation acts to enable operations to be carried on in specific localities that cannot be carried on anywhere else. "The great purpose of the provision," said Graves, J., "was to introduce a system of legislation in regard to the institution of corporations which would exclude the corruption and party favoritism which had too often accompanied the method previously in vogue, and to secure, as far as practicable, for all the people of the state, an equality of opportunity and a guard against sectional discriminations. It was determined that corporations of the class in question should owe their erection to general laws, and not to special acts, and, within this principle, that no law, general in form, should be allowed to localize the specific work or business of the corporation within narrower bounds than it would naturally be bound to occupy if not thus localized by enactment. At the same time, it was not designed to hinder the confinement of the specific work or business of the corporation, by the terms of the law, within a given section, in any case when, in consequence of natural conditions, such work or business could not be carried on elsewhere."

⁴⁶ 1 *Thomp. Corp.* § 593, 598; *Atlantic City Waterworks Co. v. Consumers' Water Co.*, 44 N. J. Eq. 427, 15 Atl. 581; *Weinman v. Railway Co.*, 118 Pa. St. 192, 12 Atl. 288; *Thomas v. Railway Co.*, 40 Fed. 126. In *Frye v. Partridge*, 82 Ill. 267, an act for establishing a single ferry at a designated point on a particular river was held void as a local and special act.

⁴⁷ *City and County of San Francisco v. Spring Valley Waterworks*, 48 Cal. 493; *Belleville & I. R. Co. v. Gregory*, 15 Ill. 20.

⁴⁸ *Carpenter v. People*, 8 Colo. 116, 5 Pac. 828; *Gentile v. State*, 29 Ind. 409; *State v. Hitchcock*, 1 Kan. 178; *Knowles v. Board of Education*, 33 Kan. 692, 7 Pac. 561; *State v. County Court*, 50 Mo. 317; *Evans v. Job*, 8 Nev. 322. Contra, *State v. Mayor, etc., of Newark*, 40 N. J. Law, 71; *Ex parte Pritz*, 9 Iowa, 30; *Von Phue v. Hammer*, 29 Iowa, 222; *Thomas v. Board of Com'rs*, 5 Ind. 4 (since overruled). In several states the question is expressly left to the judgment of the legislature. *People v. Bowen*, 21 N. Y. 517. It was formerly so in Illinois. *Johnson v. Railroad Co.*, 23 Ill. 202.

Constitutional prohibitions against creating corporations, or granting corporate powers, by special act, are not to be construed as retrospective, so as to render invalid and take away a previous grant of corporate powers to corporations organized and in actual operation.⁴⁹

RATIFICATION OF CLAIM TO CORPORATE EXISTENCE.

21. Recognition and ratification by the legislature of a claim of corporate existence render the body a corporation. But where the claim is wholly without authority, and the constitution prohibits the creation of corporations by special act, recognition and ratification by special act are not effectual.

Express ratification by the legislature of a claim to corporate existence, or an implied ratification by recognition of the claim and of the pretended corporation as a legally existing one, as by empowering it to do acts which only a corporate body can do, renders the body a legal corporation as fully as if originally created by the legislature; and this is true even where the claim is without any authority whatever.⁵⁰ And such a ratification relates back, and renders previous acts of the body as a corporation valid corporate acts.⁵¹ In like manner, failure to comply with conditions precedent in an attempted organization of a corporation under an act of the legislature may be waived by the legislature, and so cured, in the

⁴⁹ *State v. Illinois Cent. R. Co.*, 33 Fed. 730, 769.

⁵⁰ *Jameson v. People*, 16 Ill. 257; *Illinois G. T. R. Co. v. Cook*, 29 Ill. 237; *People v. Farnham*, 35 Ill. 562; *Mitchell v. Deeds*, 49 Ill. 416; *Basshor v. Dressel*, 34 Md. 503; *Attorney General v. Joy*, 55 Mich. 94, 20 N. W. 806; *St. Louis R. Co. v. Northwestern St. L. Ry. Co.*, 2 Mo. App. 69; *People v. Perrin*, 56 Cal. 845; *Williams v. Bank*, 2 Humph. (Tenn.) 339; *Society for Propagation of Gospel in Foreign Parts v. Town of Pawlet*, 4 Pet. 480, 501; *Atlantic & P. R. Co. v. City of St. Louis*, 66 Mo. 228; *Boykin v. State*, 96 Ala. 16, 11 South. 66; *McDougald v. Bellamy*, 18 Ga. 411; *State v. Webb* (Ala.) 20 South. 462. Compare *People v. Kingston & M. Turnpike Road Co.*, 23 Wend. (N. Y.) 193, 35 Am. Dec. 551. An act amending the charter of an alleged corporation, being a recognition of its corporate existence, cures any defects in the original incorporation. *Snell v. City of Chicago*, 133 Ill. 413, 24 N. E. 532.

⁵¹ See the cases cited above

case of any particular corporation, by a statute expressly approving and ratifying its organization, or impliedly doing so by recognizing it as valid.⁵² To constitute a ratification of a claim to corporate existence, it must, of course, clearly appear that the legislature intended to recognize the corporation as existing.⁵³

As was stated in a former section, a special act waiving a failure to comply with conditions precedent in the attempted organization of a corporation under a general law is not a violation of the constitutional prohibition against the "creation" of corporations by special act; but it is otherwise if the legislature, by special act, attempts to ratify a claim to corporate existence that is altogether unauthorized.⁵⁴

INTENTION TO CREATE A CORPORATION.

22. No particular form of words is necessary to the creation of a corporation. All that is necessary is that such an intention on the part of the legislature shall clearly appear from the act.

In creating a corporation the legislature generally uses language which admits of no doubt, as the words "incorporate," "found," "erect," etc.; but no particular form of words is ever necessary. It was so held in *Sutton's Hospital Case*,⁵⁵ and the same principle has been declared in numerous cases since that time. All that is necessary is that it shall appear that the legislature intended to create a corporation. Such an intention is shown whenever all the powers and faculties essential to the existence of a corporation are conferred, though the words "corporation" or "incorporate" are not used in the statute.⁵⁶ "Whenever it is apparent that the intention of the

⁵² *Central Agricultural & Mechanical Ass'n v. Alabama Gold Life Ins. Co.*, 70 Ala. 120; *McAuley v. Railway Co.*, 83 Ill. 348; *Kanawha Coal Co. v. Coal Co.*, Fed. Cas. No. 7,606.

⁵³ *Thornton v. Railway Co.*, 123 Mass. 32, 1 Cumming, Cas. Priv. Corp. 462; *Green v. Seymour*, 3 Sandf. Ch. (N. Y.) 285.

⁵⁴ Ante, p. 46, and cases there cited.

⁵⁵ 10 Coke, 30, 2 Cumming, Cas. Priv. Corp. 14.

⁵⁶ *Thomas v. Dakin*, 22 Wend. (N. Y.) 9, 1 Cumming, Cas. Priv. Corp. 1; *Conservators of River Tone v. Ash*, 10 Barn. & C. 349, 1 Cumming, Cas. Priv. Corp. 23; *Dean v. Davis*, 51 Cal. 406; *Mahony v. Bank of State*, 4 Ark. 620.

legislature will be defeated if certain parties are not found to possess corporate powers, they will be held to be created a corporation.”⁵⁷ Thus, a grant to certain persons by the state, of property or powers which they cannot hold or exercise unless they have a corporate character, will confer such a character.⁵⁸ If no intention to create a body corporate is expressed, and the powers conferred may be exercised as well by an unincorporated association, an intention to create a corporation will not be inferred.⁵⁹

AGREEMENT BETWEEN CORPORATION AND STATE—ACCEPTANCE OF CHARTER.

23. It is essential to the formation of a private corporation that there shall be consent on the part of the persons composing it, as well as on the part of the state. There must be an agreement between the corporators in their collective capacity, or the corporation, and the state. Therefore—

- (a) When a charter is offered by the legislature, it must be accepted, to have any effect.
- (b) Until acceptance, the state may withdraw the offer, as by repeal of the law, or adoption of a constitutional provision rendering it void.

⁵⁷ *Bow v. Allenstown*, 34 N. H. 351.

⁵⁸ *Bow v. Allenstown*, *supra*; *Dean v. Davis*, 51 Cal. 410; *Dunn v. University*, 9 Or. 357; *Town of North Hempstead v. Town of Hempstead*, 2 Wend. (N. Y.) 109. “Whenever the language manifests the intention of the government to confer corporate privileges, they may be conferred without the adoption of any particular technical phraseology or minutely descriptive language. It is indeed a principle of law that has been often acted on, that where rights, privileges, and powers are granted by law to an association of persons by a collective name, and there is no mode by which such rights can be enjoyed, or such powers exercised, without acting in a corporate capacity, such associations are, by implication, a corporation, so far as to enable them to exercise the rights and powers granted.” *Ang. & A. Corp.* §§ 77, 78.

⁵⁹ Thus, where the executive council of Massachusetts passed a resolution as follows: “Advised, that a company of artillery be established by Watertown, agreeable to military law,”—it was held that the intention to make the company a corporation could not be inferred. *Shelton v. Banks*, 10 Gray (Mass.) 401. And see *Stebbins v. Jennings*, 10 Pick. (Mass.) 172.

(c) The offer will lapse because not accepted within a specified time, or within a reasonable time where no time is specified.

(d) The charter must be accepted, if at all, unconditionally and according to its terms, and by those persons to whom it is made.

(e) In the absence of provision to the contrary, acceptance of a charter may be presumed from acts of the corporators; and it will be presumed where they organize, and proceed to execute the powers conferred.

24. The above rules apply equally to acts of the legislature amending existing charters.

It is commonly said that corporations are created by an act of the sovereign,—in this country, by an act of the legislature,—and in a sense this is true. But it is not to be understood from this that the legislature can bring a private corporation into existence of its own accord, and without the consent of the members who compose it. The consent of the legislature is absolutely essential to the existence of a corporation; but it is equally essential, in the case of private corporations, that there shall be consent upon the part of the persons incorporated. The charter of a private corporation is a contract between the corporation and the state; and we may therefore apply to the formation of a private corporation the principles of law governing offer and acceptance in the formation of other contracts.

If persons apply to the legislature for a charter, this is sufficient evidence of consent on their part, and, when the charter is granted, no acceptance of it by them, other than will be implied from their previous application, need be shown.⁶⁰ Indeed, they may be considered as having made an offer, and the state as having accepted it. If, however, without such application, the legislature offers a charter, either to particular persons by a special act, or to persons or a class

⁶⁰ *Perkins v. Sanders*, 56 Miss. 733; *Society of Middlesex Husbandmen & Manufacturers v. Davis*, 8 Metc. (Mass.) 133; *City of Atlanta v. Gate City Gas-light Co.*, 71 Ga. 106.

of persons generally by a general law, an acceptance must be shown. Until acceptance, the offer of a charter, either by a general or a special law, can have no effect whatever.⁶¹ An act of the legislature authorizing persons to become a body corporate by complying with certain terms and conditions is, until accepted by the persons authorized, nothing but an offer on the part of the state, which may be withdrawn by it at any time; and it is withdrawn, so as to be no longer open for acceptance, by a repeal of the act by the legislature, or by the adoption of a constitutional provision rendering such an act void.⁶²

It is also the rule in the formation of corporations, as it is in the formation of contracts generally, that the offer of a charter by the state must be accepted according to its terms. It cannot be accepted conditionally or on terms varying from the offer, nor can it be accepted in part and rejected in part, unless this is allowed by the act.⁶³ On the same principle, the offer, if made to particular persons, must be accepted by them. It cannot be accepted by others, nor by a part, only, of those to whom it is offered.⁶⁴ General laws authorizing the formation of corporations are general offers to any persons who may bring themselves within their provisions. If conditions precedent are prescribed in the statute, or certain acts are re-

⁶¹ *State v. Dawson*, 16 Ind. 40, 1 Cumming, Cas. Priv. Corp. 65, W. D. Smith, Cas. Corp. 19, Shep. Cas. Corp. 54; *Smith v. Silver Val. Min. Co.* (Md.) 20 Atl. 1032; *Bagg's Case*, 1 Rolle, 224; *Hammond v. Jethro*, 2 Brownl. & G. 100; *Rex v. Amery*, 1 Term R. 575; *Rutter v. Chapman*, 8 Mees. & W. 25; *Falconer v. Campbell*, Fed. Cas. No. 4,620; *Ellis v. Marshall*, 2 Mass. 269; *Yeaton v. Bank of Old Dominion*, 21 Grat. (Va.) 593; *President, etc., of Lincoln & Kennebec Bank v. Richardson*, 1 Greenl. (Me.) 79; *Shortz v. Unangst*, 3 Watts & S. (Pa.) 45; *Haslett's Ex'rs v. Wotherspoon*, 1 Strobb. Eq. (S. C.) 209; *Willis v. Chapman* (Vt.) 35 Atl. 459. "The mere grant of a charter, where it does not appear upon the face of the incorporating act, or otherwise, that the named corporators applied for it, does not create the corporate body. Something more must be done. There must be at least an acceptance of the grant by a majority of the corporators before corporate life and existence can begin." Per Miller, J., in *Smith v. Mining Co.*, supra.

⁶² *State v. Dawson*, supra; *Aspinwall v. Daviess County Com'rs*, 22 How. 364; *Gillespie v. Railroad Co.*, 17 Ind. 243.

⁶³ *Rex v. Westwood*, 4 Barn. & C. 781, 7 Bing. 1; *Lyons v. Railroad Co.*, 32 Md. 18, 29.

⁶⁴ Ang. & A. Corp. 25; Cook, Stock. Stockh. & Corp. Law, § 649; Mor. Priv. Corp. § 22; *Rex v. Amery*, 1 Term R. 589.

quired to be done, they are terms of the offer, and must be complied with.⁶⁵ The state's offer of a charter, like the offer in the formation of an ordinary contract, must be accepted within the time specified in it, or, if no time for acceptance is specified, it must be accepted within a reasonable time. If it is not so accepted, the offer will lapse, and will be no longer open for acceptance.⁶⁶

The acceptance of a charter may be inferred from the acts of the incorporators, or a majority of them; and a written instrument or note of acceptance is not indispensable, unless made so by the terms of the act.⁶⁷ Any act on the part of the incorporators, which shows an unequivocal intention to accept, is sufficient; as, for instance, where they proceed to execute the powers conferred by the charter offered them.⁶⁸ If such acts are shown, acceptance will be presumed.⁶⁹

The rule that a charter must be accepted before it can have any effect applies to acts of the legislature extending a charter that has expired, or is about to expire.⁷⁰ It also applies to acts amending existing charters under a right reserved to the state when the charter was granted;⁷¹ for, though the state may reserve the right to amend the charter of a private corporation, it cannot compel the members

⁶⁵ Post, p. 55; *Fire Department of New York v. Kip*, 10 Wend. (N. Y.) 266; *Quinlan v. Railway Co.* (Tex. Sup.) 34 S. W. 788.

⁶⁶ *State v. Bull*, 16 Conn. 179; *Bonaparte v. Railroad Co.*, 75 Md. 840, 28 Atl. 784.

⁶⁷ *Rex v. Amery*, 1 Term R. 575; *Bank of U. S. v. Dandridge*, 12 Wheat. 64, 70; *Gleaves v. Turnpike Co.*, 1 Sneed (Tenn.) 491.

⁶⁸ See, in addition to the cases cited above, *Demarest v. Flack*, 128 N. Y. 205, 28 N. E. 645; *State v. Montgomery Light Co.*, 102 Ala. 594, 15 South. 347; *Jackson v. Walsh*, 75 Md. 304, 23 Atl. 778; *St. Joseph & I. R. Co. v. Shambaugh*, 106 Mo. 557, 17 S. W. 581; *Com. v. Cullen*, 13 Pa. St. 133; *Russell v. McLellan*, 14 Pick. (Mass.) 63; *Society of Middlesex Husbandmen & Manufacturers v. Davis*, 3 Metc. (Mass.) 133; *McKay v. Beard*, 20 S. C. 156. Signing the articles of association, and complying with all the other requirements of a general law authorizing the formation of corporations, is clearly sufficient evidence of acceptance. *Glymont Imp. & Exc. Co. v. Toler*, 80 Md. 278, 30 Atl. 651; *Benbow v. Cook*, 115 N. C. 824, 20 S. E. 453.

⁶⁹ *Bank of U. S. v. Dandridge*, 12 Wheat. 64, 70.

⁷⁰ *President, etc., of Lincoln & Kennebec Bank v. Richardson*, 1 Greenl. (Me.) 79.

⁷¹ *Com. v. Cullen*, 13 Pa. St. 133; *Yeaton v. Bank*, 21 Grat. (Va.) 598; post, p. 213.

to accept the charter as amended, any more than it could compel them to accept the original charter. If they do not choose to adopt the amendment, they may give up their charter altogether. The acceptance of an amendment, like the acceptance of an original charter, may be implied from the conduct of the corporation or its members, and it will be conclusively presumed if the powers conferred by the amendatory act are exercised.⁷³

The acceptance of an amendatory act, as we shall see, must generally be by the shareholders, and not by the board of directors. It must be so if it changes the constitution of the corporation. Thus, if an act of the legislature authorizes a corporation to increase its capital stock, the directors cannot make the increase without the assent of the shareholders.⁷³ If, however, action by the stockholders is not required by the act itself, and the act merely grants an additional privilege which is within the scope of the general authority of the board of directors,—as, where an act authorizes a railroad company to take, for a station, land belonging to another railroad company, and the by-laws vest in the directors the power to take lands and locate stations,—it has been held that their acts alone will be sufficient evidence of acceptance.⁷⁴

PLACE OF ORGANIZATION.

25. The acceptance of the charter by the corporators, and other acts necessary to the organization of the corporation, must take place within the state.

⁷³ *Com. v. Cullen*, supra. And see *Jackson v. Walsh*, 75 Md. 304, 23 Atl. 778; *Illinois River R. Co. v. Zimmer*, 20 Ill. 654; *Owen v. Purdy*, 12 Ohio St. 78; ante, p. 53, and cases there cited in notes 67–69. In *Miller v. Insurance Co.*, 92 Tenn. 167, 21 S. W. 39, it was held that an insurance company, by issuing policies and continuing business after an act amending the charters of such companies, passed in pursuance of a right of amendment reserved to the state in the general incorporation law, which amendment the company was therefore bound to adopt if it wished to continue business, thereby accepted the amendment.

⁷³ *Eldman v. Bowman*, 58 Ill. 444; *Chicago City Ry. Co. v. Allerton*, 18 Wall. 233.

⁷⁴ *Eastern R. Co. v. Boston & M. R. Co.*, 111 Mass. 125. As to the power of directors, see post, p. 485.

The officers of a corporation may perform acts as agents of the corporation outside of the state of its creation, unless prohibited by local legislation; but no strictly corporate act can be done outside of the state.⁷⁵ The reason is, as we shall presently show, that a corporation can have no legal existence outside of the boundaries of the sovereignty by which it was created.⁷⁶ Acceptance of a charter, and organization under it, are strictly corporate acts, and must, to be effective, take place within the state. Thus, where a charter was granted by the state of North Carolina, and the incorporators, who were authorized to act as directors until others should be elected, assembled in Baltimore, and there passed resolutions of acceptance, and performed the other acts necessary to organize the corporation, it was held that the proceedings were void, and that the pretended corporation had no legal existence.⁷⁷

COMPLIANCE WITH CONDITIONS PRECEDENT.

26. Where the law authorizing the formation of a corporation prescribes formalities to be observed as conditions precedent to becoming a corporation, a compliance therewith is essential to the legal existence of a corporation. But

- (a) A substantial compliance is sufficient.**
- (b) The legal existence of a corporation is not affected by noncompliance with provisions that are merely directory, and not mandatory.**

⁷⁵ *Miller v. Ewer*, 27 Me. 509; *Freeman v. Mill Co.*, 88 Me. 848; *Smith v. Mining Co.*, 64 Md. 85, 20 Atl. 1032.

⁷⁶ *Post*, p. 74.

⁷⁷ *Smith v. Mining Co.*, 64 Md. 85, 20 Atl. 1032. And see *Miller v. Ewer*, 27 Me. 509. Compare *Ohio & M. R. Co. v. McPherson*, 35 Mo. 13. In *Glymont Imp. & Exc. Co. v. Toler*, 80 Md. 278, 30 Atl. 651, it was held that, though the directors of a corporation held their first meeting and organized outside the state, organization within the state was shown by the fact that ever since its incorporation the incorporators and their successors had exercised corporate rights of every kind under the charter, had issued certificates of stock under the corporate seal, had expended money in developing its property, that a board of directors had been annually elected by the stockholders within the state, and the directors so elected controlled and managed the property and affairs of the corporation.

- (c) Nor is it affected by noncompliance with conditions subsequent. This includes conditions precedent to the right to do business, which are not intended as conditions precedent to incorporation.
- (d) A corporation de facto may exist notwithstanding noncompliance with conditions precedent; and in such a case the existence of the corporation can only be questioned by the state, and in a direct proceeding brought for that purpose.
- (e) A person may be estopped from denying that an association is a corporation by dealing with it, or holding it out, as a corporation.

Since it lies entirely with the state whether it will create a corporation or not, it has a right to impose any conditions it may see fit in the charter or act authorizing incorporation, and a substantial compliance therewith by the incorporators is essential to the legal existence of a corporation. In *Attorney General v. Hanchett*⁷⁸ a Michigan statute declared that whenever the common council of a city should, by resolution, declare that it was expedient to have water works constructed, but that it was inexpedient for the city to construct such works, it should be lawful for private individuals to organize a water company in the manner therein set forth. The defendants sought to organize a corporation under this statute, and assumed to act as such, without any resolution as required by the statute. In proceedings by the state, the defendants were ousted from the exercise of corporate powers on the ground that such a resolution by the common council of the city was a condition precedent to the legal existence of a corporation under the statute. And so it has been held where the statute required that there should be a certain number of associates;⁷⁹ that there should be written articles of agreement between the incorporators;⁸⁰ that the articles of associa-

⁷⁸ 42 Mich. 436, 4 N. W. 182.

⁷⁹ *Montgomery v. Forbes*, 148 Mass. 249, 19 N. E. 842, and 1 Cumming, Cas. Priv. Corp. 69; *State v. Critchett*, 37 Minn. 18, 32 N. W. 787; *Broderip v. Solomon* [1895] 2 Ch. 323.

⁸⁰ *Utleigh v. Tool Co.*, 11 Gray (Mass.) 189; *Unity Ins. Co. v. Oram*, 43 N. H. 636. Where the statute requires written articles of association, "it is obvious that the three or more persons must sign and execute these articles in such a

tion should set forth certain facts;⁸¹ that they should be subscribed by the corporators,⁸² and acknowledged by them;⁸³ that the articles or a certificate should be recorded or filed in a certain court or office;⁸⁴ that notice of organization, setting forth certain facts, should be published.⁸⁵

manner as to come within the well-established rules of law prescribing the elements necessary to constitute a signing or execution which will make the paper executed the legal and binding instrument of the person who executes it. Their signatures must not be procured, without fault on their part, by fraud; nor must they be affixed with the understanding and upon condition that the paper signed is not to take legal effect, and be valid and binding, either presently, or at some fixed and definite time, or upon the happening of some contingency or fulfillment of some condition within the bounds of possibility. Nor is it obvious how such an instrument as this, more than any other, can have life and binding force, if executed only to take effect upon the happening of some event, unless it is shown that the event has happened." *Corey v. Morrill*, 61 Vt. 598, 17 Atl. 840.

⁸¹ As that they should set forth the number of directors and their names, *Reed v. Railway Co.*, 50 Ind. 842; or that they should give the names and places of residence of the subscribers to stock, *Busenback v. Road Co.*, 43 Ind. 265; *Miller v. Road Co.*, 52 Ind. 51; or should state the manner of carrying on the business, *State v. Central Ohio Mut. Relief Ass'n*, 29 Ohio St. 399; or the place of carrying on the business, *Harris v. McGregor*, 29 Cal. 124; *Montgomery v. Forbes*, 148 Mass. 249, 19 N. E. 342, 1 Cumming, Cas. Priv. Corp. 69; or the purposes of the incorporation, *West v. Ditching Co.*, 32 Ind. 138; *O'Reiley v. Draining Co.*, Id. 169; *Attorney General v. Lorman*, 59 Mich. 157, 26 N. W. 311; *In re Crown Bank*, 44 Ch. Div. 634; or the fact that a majority of the associates were present and voted at the election of directors, *People v. Selfridge*, 52 Cal. 331. The fact that the articles claim more than the act allowed does not vitiate them so as to prevent the corporation from coming into existence. The excessive claims may be rejected as surplusage. *Eastern Plank-Road Co. v. Vaughan*, 14 N. Y. 546; *Shick v. Enterprise Co.* (Ind. App.) 44 N. E. 48; *post*, p. 58.

⁸² *Kaiser v. Bank*, 56 Iowa, 104, 8 N. W. 772. Articles may be signed by the corporators by their usual signatures, and the use of initials to designate their Christian names is not objectionable. *State v. Beck*, 81 Ind. 500.

⁸³ *Doyle v. Mizner*, 42 Mich. 332, 8 N. W. 968; *Kaiser v. Bank*, 56 Iowa 104, 8 N. W. 772. If the statute requires that five persons shall subscribe the articles, and that they shall be acknowledged by each, articles subscribed by five persons, but acknowledged by four only, are not sufficient. *People v. Montecito Water Co.*, 97 Cal. 276, 32 Pac. 236. The notary's certificate of acknowledgment of the articles need not show that the persons acknowledging the same are personally known to him. *People v. Cheeseman*, 7 Colo. 376, 3 Pac. 716.

⁸⁴ *Abbott v. Smelting, etc., Co.*, 4 Neb. 416; *Kaiser v. Bank*, 56 Iowa, 104,

⁸⁵ *Clegg v. Grange Co.*, 61 Iowa, 121, 15 N. W. 865.

Sometimes, subscriptions to stock to a certain amount are required as a condition precedent;⁸⁶ and it is sometimes required that a certain percentage of the stock subscribed shall be paid up, or shall be paid in cash.⁸⁷ In the absence of such a requirement in the statute, subscriptions to stock are not a condition precedent to corporate existence; but the corporation may be organized, and the stock, or part of it, may be subscribed afterwards.⁸⁸ Illustrations of conditions precedent might be multiplied almost indefinitely.⁸⁹ The fact that the articles of association claim more than the law

8 N. W. 772; *Childs v. Hurd*, 82 W. Va. 68, 9 S. E. 362; *Bigelow v. Gregory*, 73 Ill. 197; *Hurt v. Salisbury*, 55 Mo. 311; *Walton v. Riley*, 85 Ky. 413, 3 S. W. 605; *Loverin v. McLaughlin* (Ill. Sup.) 44 N. E. 99. Compare *Granby Mining & Smelting Co. v. Richards*, 95 Mo. 106, 8 S. W. 246. As to filing copy with the secretary of state, see *First Nat. Bank v. Davies*, 43 Iowa, 424; *Indianapolis F. & M. Co. v. Herkimer*, 46 Ind. 142; *Garnett v. Richardson*, 35 Ark. 144. And compare *Mokelumne Hill Canal & Mining Co. v. Woodbury*, 14 Cal. 424; *Walton v. Riley*, 85 Ky. 413, 3 S. W. 605. The corporation, under some statutes, comes into existence before filing the certificate, filing the certificate being required as evidence of the corporate existence, which dates from the time fixed in the certificate. See *Vanneman v. Young*, 52 N. J. Law, 403, 20 Atl. 53.

⁸⁶ See post, p. 308; *People v. Chambers*, 42 Cal. 201; *Sweney v. Talcott*, 85 Iowa, 103, 52 N. W. 106; *Lake Ontario, A. & N. Y. R. Co. v. Mason*, 16 N. Y. 451; *Franklin Fire Ins. Co. v. Hart*, 31 Md. 59. In *Holman v. State*, 105 Ind. 569, 5 N. E. 702, it was held that where the state, by quo warranto, directly challenged the right of persons to act as a corporation, and it appeared that many of the subscribers for the stock were notoriously insolvent, and had no expectation, at the time they subscribed, of ever paying their subscription, thus leaving the amount subscribed in good faith less than that required by the statute, a judgment of ouster was proper.

⁸⁷ *People v. Chambers*, 42 Cal. 201.

⁸⁸ *Perkins v. Sanders*, 56 Miss. 733; *Hammond v. Straus*, 53 Md. 1; *Proprietors of City Hotel v. Dickinson*, 6 Gray (Mass.) 586; *Minor v. Bank*, 1 Pet. 46; *Johnson v. Kessler*, 76 Iowa, 411, 41 N. W. 57; *National Bank v. Texas Inv. Co.*, 74 Tex. 421, 12 S. W. 101; *Singer Manuf'g Co. v. Peck* (S. D.) 67 N. W. 947.

⁸⁹ See *Capps v. Prospecting Co.*, 40 Neb. 470, 58 N. W. 956; *Martin v. Deetz*, 102 Cal. 55, 36 Pac. 368; *Heinig v. Manufacturing Co.*, 81 Ky. 300. A certificate of incorporation, which provides that the corporate affairs shall be controlled by its president, vice president, and attorney, instead of providing for a board of directors, or trustees, as required by the statute, is insufficient to create a corporation de jure. *Bates v. Wilson*, 14 Colo. 140, 24 Pac. 99.

allows does not render the incorporation invalid, if the excessive part of the claim can be rejected as surplusage.⁹⁰

Substantial Compliance with the Statute is Sufficient.

In organizing a corporation under either a general or a special law, only a substantial compliance with the provisions of the statute is required, even as against the state. Thus, it has been held that the organization of a corporation is sufficient where the requirements of the statute are all observed, but not in the order prescribed;⁹¹ that, where the statute requires the directors to be named in the articles of association, it is a sufficient compliance with the statute if the articles are adopted at the time of electing directors.⁹² Many other cases may be cited to the same effect.⁹³ As was said in a California case, however: "Because a substantial compliance will do, it does not follow that any positive statutory requirement can be omitted, on the ground that it is unimportant. They are conditions precedent to acquiring a statutory right, and none can be dispensed with by the court."⁹⁴

⁹⁰ 1 Thomp. Corp. § 229; *People v. Cheeseman*, 7 Colo. 376, 3 Pac. 716. In this case, under a statute incorporation for the period of 20 years, the articles of association provided for a corporate existence for 50 years. The court held that the corporation could exist for 20 years. See ante, p. 57, note 81.

⁹¹ *Eakright v. Railroad Co.*, 13 Ind. 404.

⁹² *Eakright v. Railroad Co.*, supra.

⁹³ *Roman Catholic Orphan Asylum v. Abrams*, 49 Cal. 455; *People v. Stockton & V. R. Co.*, 45 Cal. 306, 313; *Oroville & V. R. Co. v. Supervisors of Plumas Co.*, 37 Cal. 354; *Thornton v. Balcom*, 85 Iowa, 198, 52 N. W. 190; *State v. Wood*, 13 Mo. App. 139, 84 Mo. 378; *Buffalo & P. R. Co. v. Hatch*, 20 N. Y. 157; *Rogers v. Society*, 19 Vt. 187. Failure of the notary's certificate of acknowledgment of articles of association to show that the persons acknowledging the same were personally known to him. *People v. Cheeseman*, 7 Colo. 376, 3 Pac. 716. In *State v. Wood*, supra, it was held that a statutory requirement that one-half of the capital stock shall be "actually paid up in lawful money of the United States," is substantially complied with if the corporation has property the market value of which is greater than the par value of the stock.

⁹⁴ *People v. Water Co.*, 97 Cal. 276, 32 Pac. 236. In this case the statute required the articles of association to be subscribed by five or more persons, and acknowledged by each. It was held that where five persons subscribed the articles, but only four persons acknowledged them, there was not a substantial compliance. For other cases on this point, see *Olegg v. Grange Co.*, 61 Iowa, 121, 15 N. W. 865. In *State v. Association*, 29 Ohio St. 399, it was held that a cer-

Provisions That are Merely Directory.

It is not every provision in a charter or act of incorporation setting out formalities to be observed that is to be regarded as mandatory, so that a compliance therewith will be held a condition precedent. If the provision is merely directory, failure to comply with it will not be fatal. Whether a particular provision is mandatory or merely directory must be determined by ascertaining the intention of the legislature, to be gathered from the statute and its purpose; and in the cases on this point we must expect to find some conflicting decisions. The distinction may be illustrated by two Massachusetts cases. In the first (*Utley v. Union Tool Co.*),¹¹ the alleged corporation was an association which had undertaken to assume corporate powers under a statute authorizing three or more persons, who had entered into "articles of agreement in writing" for the transaction of certain kinds of business, to organize in a manner prescribed by the statute, and thereby become a corporation. The court held that written articles of agreement were essential to constitute a corporation, and that these articles must fix the amount of the capital stock, and set forth distinctly the purpose for which, and the place in which, the corporation was established. "There is an obvious reason," it was said, "for making such organization by written articles of agreement a condition precedent to the exercise of corporate rights. It is the basis on which all subsequent proceedings are to rest, and is designed to take the place of a charter or act of incorporation, by which corporate rights and privileges are usually granted." On the other hand, in *Newcomb v. Reed*,¹² where an act of incorporation provided that the first meeting should be called by a majority of the persons named in the act of incorporation, it was held that this provision was merely di-

tificate of incorporation setting forth that "the manner of carrying on the business shall be such as the association shall from time to time prescribe by rules, regulations, and by-laws, not inconsistent with the laws of the state," was not a substantial compliance with a requirement that the certificate should show "the manner of carrying on the business of said association." And see *In re Crown Bank*, 44 Ch. Div. 634.

¹¹ 11 Gray (Mass.) 139, and cases heretofore cited.

¹² 12 Allen (Mass.) 362, 1 Cumming, Cas. Priv. Corp. 67.

rectory, and a failure to comply therewith did not prevent the corporation from coming into existence.⁹⁷

Present Grant with Conditions Subsequent—Conditions Precedent to Doing Business.

Acts authorizing the formation of a corporation, and prescribing conditions precedent to its coming into existence, must be distinguished from acts creating a corporation, and giving it a present corporate existence, but prescribing conditions to be subsequently complied with. In the latter case, acceptance of the grant is all that is necessary to the creation of a corporation. Noncompliance with a condition subsequent does not affect the existence of the corporation, though it may be ground for a proceeding by the state to forfeit the charter. An act of the legislature of Missouri, incorporating a railroad company, declared that "a company is hereby created, called the 'St. Joseph & Iowa Railroad Company,'" and designated the first board of directors, but imposed no conditions precedent. It did provide, however, that the directors should meet and organize as a board of directors, and open books for subscriptions to stock, and fixed a time within which the company should commence and complete its road. It was held that these were merely conditions subsequent; that the act was a present grant of corporate powers; and that the corporation came into existence on acceptance of the charter.⁹⁸

Conditions precedent to the formation of a corporation must be distinguished from conditions precedent to the right to engage in business after the corporation has been formed. The latter are conditions subsequent, a noncompliance with which, while it may give the state a right to maintain proceedings to forfeit the char-

⁹⁷ See, also, *Walworth v. Brackett*, 98 Mass. 98; *Gross v. Mill Co.*, 17 Ill. 54; *Proprietors of City Hotel in Worcester v. Dickinson*, 6 Gray (Mass.) 586, 593; *Elakright v. Railroad Co.*, 13 Ind. 404; *Humphreys v. Mooney*, 5 Colo. 282; *Braintree Water-Supply Co. v. Town of Braintree*, 146 Mass. 482, 16 N. H. 420.

⁹⁸ *St. Joseph & I. R. Co. v. Shambaugh*, 106 Mo. 557, 17 S. W. 582. See, also, *Cheraw & C. R. Co. v. White*, 14 S. C. 51; *Toledo & Ann Arbor R. Co. v. Johnson*, 49 Mich. 148, 13 N. W. 492. For other illustrations of conditions subsequent, see *Boston Acid Manuf'g Co. v. Moring*, 15 Gray (Mass.) 211; *Schenectady & Saratoga Plank-Road Co. v. Thatcher*, 11 N. Y. 102; *Merrick v. Governor Co.*, 101 Mass. 381.

ter, does not, in the absence of such proceedings, in any way affect the legal existence of the corporation. The case of *Harrod v. Hammer*⁹⁹ illustrates this distinction. A statute of Wisconsin provided that, before any corporation organized thereunder should "commence business," the officers should cause the articles of association to be published in the papers, make a certificate setting forth the purpose for which the corporation was formed and certain other facts, and deposit the same with certain public officers. It was held that a failure to comply with these conditions did not affect the legal existence of the corporation.¹⁰⁰ "There is a broad and obvious distinction between such acts as are declared to be necessary steps in the process of incorporation, and such as are required of the individuals seeking to become incorporated, but are not made prerequisites to the assumption of corporate powers. In respect to the former, any material omission will be fatal to the existence of the corporation, and may be taken advantage of collaterally, in any form in which the fact of incorporation can properly be called in question. In respect to the latter, the corporation is responsible only to the government, and in a direct proceeding to forfeit its charter."¹⁰¹

Who may Object—Corporation de Facto—Estoppel.

While conditions precedent must always be performed, in order that a corporation may have a legal existence, it does not, by any means, follow that objection to the existence of a corporation on this ground can be raised by any and every person, and in every proceeding. The objection may always be raised by the state in a direct proceeding, brought by it to test the right to corporate existence, as in quo warranto proceedings, or proceedings in the na-

⁹⁹ 32 Wis. 162.

¹⁰⁰ See, also, *In re Shakopee Manufg Co.*, 37 Minn. 91, 33 N. W. 219; *Baker v. Backus' Admr.*, 32 Ill. 79; *Lord v. Association*, 37 Md. 320; *Hammond v. Straus*, 53 Md. 1, 11; *Holmes v. Gilliland*, 41 Barb. (N. Y.) 568; *Hughesdale Manufg Co. v. Vanner*, 12 R. I. 491; *Granby Mining & Smelting Co. v. Richards*, 95 Mo. 106, 8 S. W. 246; *Sparks v. Steel Co.*, 87 Ala. 294, 6 South. 195; *Portland & G. Turnpike Co. v. Bobb*, 88 Ky. 226, 10 S. W. 794. But see *Bigelow v. Gregory*, 73 Ill. 197; *Hurt v. Salisbury*, 55 Mo. 311; *Misfeld v. Kenworth*, 50 Iowa, 389.

¹⁰¹ *Mokelumne Hill Canal Min. Co. v. Woodbury*, 14 Cal. 424; *Hyde v. Doe*, 4 Sawy. 133, Fed. Cas. No. 6,969.

ture of quo warranto.¹⁹² Even the state, however, cannot always raise the objection; and there are many cases in which private individuals cannot object at all, though in a direct proceeding by the state it might be held that there was no legal incorporation.

We shall presently see, at some length, that if there has been a bona fide attempt to incorporate, under a law authorizing incorporation, and the law has been so far complied with as to make the association what is called a "corporation de facto," the only way in which its corporate existence can be questioned is in a direct proceeding by the state, brought for that purpose. Private individuals cannot raise the objection in such a case, either directly or indirectly, and even the state cannot raise the objection collaterally. If failure to comply with conditions precedent prevents the coming into existence of any corporation, either de jure or de facto, then, on principle and in reason, the question may be raised collaterally as well as directly, and by private individuals as well as by the state, unless there is something to operate as an estoppel. When a private individual, therefore, raises the objection that conditions precedent have not been complied with, the question, in the absence of elements of estoppel, is whether or not there is a corporation de facto. If there is, he cannot object; otherwise, he can.

Where there is not even a corporation de facto, a private person may, by the weight of authority, be barred from raising the objection on the ground that he is estopped by his conduct, as by having dealt with the pretended corporation as a corporation, or by having held it out to the public as a legally constituted corporation.

There is much confusion, and some direct conflict, in the decisions, on the law governing corporations de facto, and on the question of estoppel. These questions will be discussed and explained at length in a subsequent chapter.¹⁹³

¹⁹² *Attorney General v. Hanchett*, 42 Mich. 436, 4 N. W. 182; *People v. Montecito Water Co.*, 97 Cal. 276, 32 Pac. 236; *State v. Central Ohio Mut. Relief Ass'n*, 29 Ohio St. 389; *People v. Selfridge*, 52 Cal. 331; *People v. Chambers*, 42 Cal. 201.

¹⁹³ Post p. 86.

AGREEMENT BETWEEN CORPORATORS AND CORPORATION.

27. An agreement between the corporators and the corporation, creating a contractual relation between them, is essential to the creation of a private corporation.

It is essential to the existence of a private corporation that there shall be an agreement between the corporators and the corporation, creating a contractual relation between them. There can be no such thing as a corporation aggregate without members, and a person cannot become a member except by his own agreement or contract. Some writers and some of the cases say that there must be an agreement between the members, creating a contractual relation between them,¹⁰⁴ but this is inaccurate. There is no contract between individual members in the formation of a corporation. The contract is between each individual member and the whole body of members in their collective capacity, represented by the corporation; that is, between each member and the corporation. A subscription for shares, for instance, in the organization of a corporation, is not a contract between the subscriber and the other subscribers individually, but it is a contract between each subscriber and the corporate body. This subject will be explained at length in a subsequent chapter.¹⁰⁵

WHO MAY BECOME CORPORATORS.

28. Unless excluded by the statute, any person who has the capacity to enter into contracts may be a corporator.

29. If a statute provides that a certain number of persons may organize a corporation, the prescribed number of bona fide corporators is necessary. It is competent for the legislature to authorize a single individual to form and become a private corpora-

¹⁰⁴ 1 Mor. Priv. Corp. § 24. And see *Lauman v. Railroad Co.*, 80 Pa. St. 42.

¹⁰⁵ Post, p. 253.

tion; but a statute will not be construed so as to give it this effect, unless it is clearly manifest that such was the legislative intent. If the statute authorizes "any" number of persons to form a corporation, this does not authorize a single individual to incorporate.

Capacity of the Corporators.

It is an implied term in every statute authorizing the formation of corporations, and not expressly providing otherwise, that the corporators shall be persons who are sui juris, and competent to enter into a valid contract, though the statute may in terms say nothing at all about their capacity.¹⁰⁶ Thus, it is implied that the corporators shall be of full age.¹⁰⁷

Corporations are composed generally of natural persons in their natural capacity; but they may be composed of persons in their political and artificial capacity, as other corporations. In the time of Edward the Sixth, a hospital corporation was established and chartered in England, composed of the mayor, citizens, and commonalty of London; and the same is true of a number of colleges, universities, and hospitals, both in England and in this country.¹⁰⁸ The universities of Oxford and Cambridge are corporations composed of many colleges which are separate and distinct corporations. In some jurisdictions one business corporation is allowed to take shares in another.¹⁰⁹ It has been very generally held in this country, however, that, in the absence of express provision to that effect in the statute, a private business corporation cannot become a member of another corporation by subscribing for shares, as it is considered that public policy restricts the right to form a corporation to persons acting individually and in their natural capacity.¹¹⁰ And it has been held that this rule is not affected by the fact that the statute allows "persons" to incorporate; and there is another stat-

¹⁰⁶ *In re Globe Mut. Ben. Ass'n*, 68 Hun, 263, 17 N. Y. Supp. 852.

¹⁰⁷ *Id.*

¹⁰⁸ *Regents of University of Maryland v. Williams*, 9 Gill & J. (Md.) 365, 393.

¹⁰⁹ *Post*, p. 151.

¹¹⁰ *Post*, p. 151. See *Denny Hotel Co. of Seattle v. Schram*, 6 Wash. 134, 82 Pac. 1002; *Central R. Co. v. Pennsylvania R. Co.*, 31 N. J. Eq. 475.

ute declaring that the term "person" may be construed to include corporations as well as individuals, as this does not require such a construction in all cases.¹¹¹

Unless the statute expressly requires that the individuals organizing a corporation shall be residents of the state, a corporation may be formed by nonresidents, and, in so far as that state is concerned, it can make no difference that the place of business of the corporation is to be in the state of the corporators' residence.¹¹² Whether or not the corporation will be recognized as valid by the latter state is a different question, and depends upon whether such an incorporation was an evasion of, and a fraud upon, its laws.¹¹³ In most states a certain number of the corporators are required to be residents.

Number of Corporators.

Generally, the statutes authorizing the formation of corporations require expressly that there shall be at least a certain number of corporators, and such a requirement must be complied with. If less than the required number of persons attempt to organize under the statute, no corporation will come into existence.¹¹⁴ And the associates must be bona fide corporators, and not straw men.¹¹⁵

It is perhaps safe to say that there is in no state a statute authorizing a single individual to form himself into a corporate body, and thus change his status and liabilities in business transactions. It must not be supposed, however, that the state has no power to constitute a single person a private corporation. The state may, if the legislature sees fit, and there are no constitutional restrictions, grant a charter, as a private business corporation, to one man alone, and leave it optional with him whether he will associate other persons with him, or have succession without doing so. In such a case it was said: "The grant being to one person, * * * the in-

¹¹¹ Denny Hotel Co. of Seattle v. Schram, *supra*.

¹¹² Demarest v. Flack, 128 N. Y. 205, 28 N. E. 645; Lancaster v. Improvement Co., 140 N. Y. 576, 35 N. E. 964.

¹¹³ Demarest v. Flack, *supra*.

¹¹⁴ Montgomery v. Forbes, 148 Mass. 249, 19 N. E. 342, 1 Cumming, Cas. Priv. Corp. 69; Broderip v. Salomon, L. R. [1895] 2 Ch. 323; State v. Critchett, 37 Minn. 13, 32 N. W. 787.

¹¹⁵ See Broderip v. Salomon, *supra*.

ference necessarily is that it was the intention of the legislature to permit that one person or his successor to exercise all the corporate powers, and to make his acts, when acting upon the subject-matter of the corporation, and within its sphere of action and grant of power, the acts of the corporation.”¹¹⁶ A statute is not to be construed as authorizing a single individual to form and become a corporation, unless such an intention on the part of the legislature is clear. Thus, one person alone cannot organize a corporation under a statute authorizing “any number of persons” to associate themselves and become incorporated; for it is against the policy and intent of the law to permit a single individual to conduct his business in the name of and as a corporation, so as to exempt himself from the liabilities of other natural persons.¹¹⁷ Where a corporation is legally organized by the requisite number of persons, the fact that one person becomes the owner of all the shares does not dissolve it.¹¹⁸

PURPOSE OF INCORPORATION.

30. Since legislative authority is essential to a valid incorporation, the purpose for which a corporation is formed must come within the purposes authorized by the statute.

31. A corporation formed by the various manufacturers and sellers of a product, for the purpose of controlling the supply and price, and stifling competition, is contrary to public policy, and illegal.

Since there can be no valid incorporation without legislative authority, it follows that the object of a proposed corporation must be such as the statute authorizes. It is not a question whether the object is lawful or unlawful, but whether it is authorized.¹¹⁹

The difficulty in this connection, and the only difficulty, is in de-

¹¹⁶ *Penobscot Boom Corp. v. Lamson*, 16 Me. 224. And see *Day v. Stetson*, 8 Greenl. (Me.) 365.

¹¹⁷ *Louisville Banking Co. v. Elsenman*, 94 Ky. 83, 21 S. W. 531, 1049; *Swift v. Smith*, 65 Md. 428, 5 Atl. 534.

¹¹⁸ *Post*, p. 234.

¹¹⁹ *State v. International Inv. Co.*, 88 Wis. 512, 60 N. W. 798.

termining, on a construction of the statute, whether the purpose of particular associations, as set forth in the articles of association or certificate, is within the statute. Some cases are very clear. Thus, there can be no doubt or question but that a statute authorizing corporations for manufacturing purposes does not authorize a corporation for banking, or for constructing and operating a railroad. Sometimes, however, the construction of the statute and application of the rule is difficult. A statute authorizing the formation of corporations "for buying, selling, exchanging and dealing in all kinds of property, real or personal, or both," is very broad. Perhaps it might be held to authorize a manufacturing or banking corporation; but it does not authorize a corporation "to encourage frugality and economy in its members; to create, husband, and distribute funds from monthly installments, dues, or investments from its members; to purchase, take, hold, sell, convey, lease, rent, and mortgage real estate and personal property; to loan surplus accumulations; and to carry on and conduct a general investment business,"—for the primary object of such an association is to obtain money from its members, and the disposal of the money obtained by it is merely an incidental or secondary object.¹²⁰ Nor, for the same reason, is such a corporation authorized by a statute providing for the formation of corporations "for loaning money on securities or otherwise," or "for the maintenance of any benevolent or charitable institution."¹²¹ Other decisions are given below.¹²²

¹²⁰ Id.

¹²¹ Id.

¹²² A corporation to build and maintain an opera house and lecture hall is authorized by a statute allowing incorporation for the support of any educational or literary undertaking, or for the promotion of music or other fine arts. *Seymour Opera-House Co. v. Wooldridge* (Tex. Civ. App.) 31 S. W. 234. A statute allowing corporations to carry on an "industrial pursuit" authorizes corporations to carry on the express business, *Wells, Fargo & Co. v. Northern Pac. R. Co.*, 23 Fed. 469; or a mercantile business for the sale of goods, *Bashford-Burmister Co. v. Agua Fria Copper Co.* (Ariz.) 35 Pac. 983; *Carver Mercantile Co. v. Hulme*, 7 Mont. 566, 19 Pac. 213. A statute authorizing "manufacturing" companies includes electric light and gas companies. *Beggs v. Illuminating Co.*, 96 Ala. 295, 11 South. 381; *Nassau Gaslight Co. v. City of Brooklyn*, 89 N. Y. 409; *People v. Wemple*, 129 N. Y. 543, 29 N. E. 808. But see *Com. v. Northern Electric Light & Power Co.*, 145 Pa. St. 105, 22 Atl. 839. "Manufacturing" includes the production of ice by artificial means, but it has been held that it does not include the collection, storage, preparation for market, and transportation of

Where the object of an attempted incorporation cannot be brought within any of the purposes specifically mentioned in the statute, it is often sought to sustain the incorporation under a general clause contained in the statutes of most states. The construction of such clauses has given rise to conflicting decisions. In Wisconsin, a statute, after specifying certain purposes for which corporations might be formed, added the general clause, "or for any lawful business or purpose whatever." The Wisconsin court, construing this clause, held that, "by a well-settled rule of construction, these general words extend only to things of a kindred nature to those specifically authorized by the section. 'Noscitur a sociis.' Any other construction would enable parties, by mere agreement, to form a corporation for any conceivable 'business or purpose whatever,' not in violation of law. Certainly, the legislature never intended to grant such unlimited authority."¹²² This construction is certainly very

naturally formed ice. *People v. Knickerbocker Ice Co.*, 99 N. Y. 181, 1 N. E. 669. Contra, *Attorney General v. Lorman*, 59 Mich. 157, 26 N. W. 311. It also includes the manufacture of lumber, flour, and meal. *Cross v. Mill Co.*, 17 Ill. 54. A statute authorizing corporations for "manufacturing" purposes does not authorize a corporation for the purpose of carrying on a manufacturing business, and also another and independent business not properly incident to or connected with manufacturing. *State v. Minnesota Thresher Manuf'g Co.*, 40 Minn. 213, 41 N. W. 1020. A statute authorizing corporations "for the erection of buildings" was held to authorize corporations for erecting buildings as a business only. *People v. Troy House Co.*, 44 Barb. (N. Y.) 625. In *Guadalupe & S. A. R. Stock Ass'n v. West*, 70 Tex. 391, 7 S. W. 817, it was held that a corporation organized to protect the personal property of its members from violence, theft, etc., to raise money for necessary expenses by assessments, and confer with the state officers, employ counsel, police, and detectives, when necessary to the prosecution of criminals, though somewhat novel and peculiar, was authorized by a statute providing that private corporations might be formed for mutual profit or benefit, not inconsistent with the constitution and laws of the state. That an educational institution is not a corporation "for pecuniary profit," though fees are charged for tuition, see *Santa Clara Female Academy v. Sullivan*, 116 Ill. 375, 6 N. E. 183. A "mutual reliance society," constituted for pecuniary gain cannot be formed under an act for the incorporation of benevolent, charitable, scientific, and missionary societies. *People v. Nelson*, 46 N. Y. 477.

¹²² *State v. International Inv. Co.*, 88 Wis. 512, 60 N. W. 798. Even under this construction, it is held that a statute authorizing the formation of corporations for the purpose of building and operating telegraph lines, or for any other lawful business, etc., authorizes a corporation for building and operating a telephone

questionable. It is difficult to see why the legislature added this clause, and with the addition of the word "whatever," as if to emphasize, if it did not intend, as the language plainly imports, to authorize incorporation for any lawful business whatever. That such was the intention seems evident, for it could not well have been more emphatically expressed; and the rule that, when general words follow particular and specific words, the former must be confined to things of the same kind as those specifically mentioned, is only intended to aid in ascertaining the legislative intent, and not for the purpose of controlling the intention, or confining the operation of a statute within narrower limits than was intended by the lawmaker. If the intention is clearly expressed, and the language of the statute is without ambiguity, all technical rules of interpretation should be rejected.

A better decision was made by the Missouri court in construing a general clause which authorized the formation of corporations "for any other purpose intended for pecuniary profit or gain not otherwise specially provided for, and not inconsistent with the constitution and laws of this state." It was held that this authorized a corporation as the words of the clause imported, and should not be construed and limited to corporations of the kind specially mentioned in the preceding clauses.¹²⁴ And it has been held that a statute authorizing corporations "for mining, manufacturing, and other industrial pursuits" did not limit the purpose to such industrial pursuits as mining and manufacturing, but extended to the express business, or any other industrial pursuit.¹²⁵ There are many other cases in which the statute has been similarly construed.¹²⁶ The question in all cases is what was the intention of the legislature, and not what, in the opinion of the court, the legislature ought to have intended.

A corporation formed by the various manufacturers and sellers of a product, for the purpose of getting control of the manu-

line, as that is of a kindred nature. *Wisconsin Tel. Co. v. City of Oshkosh*, 62 Wis. 32, 21 N. W. 828.

¹²⁴ *State v. Corkins*, 123 Mo. 56, 27 S. W. 363.

¹²⁵ *Wells, Fargo & Co. v. Northern Pac. R. Co.*, 23 Fed. 469, 474.

¹²⁶ *York Park Bldg. Ass'n v. Barnes*, 39 Neb. 834, 58 N. W. 440; *National Bank v. Texas Inv. Co.*, 74 Tex. 421, 12 S. W. 101; *Brown v. Corbin*, 40 Minn. 508, 42 N. W. 481.

facture and sale of the product, so as to stifle competition, and control the supply and price, is illegal, as being contrary to public policy, because it creates a monopoly, and is in restraint of trade. In *Distilling & Cattle Feeding Co. v. People*,¹²⁷ in which quo warranto proceedings were brought against the defendant corporation to oust it from the exercise of corporate franchises, it appeared that a trust combination was organized in order to obtain control of the manufacture and sale of distillery products, by purchasing the stock of various distillery companies, and placing it in the hands of trustees. The trust combination was then changed into the defendant corporation, which was organized, owned, and controlled by the trustees of the combination, and all the property controlled by the combination was transferred to it. The corporation was held illegal, as creating a monopoly, and was ousted from the exercise of corporate franchises.¹²⁸

CORPORATE NAME.

32. A corporation must have a corporate name.

33. Ordinarily, the incorporators may select any name they choose. But—

(a) Sometimes there are statutory restrictions in this respect, and the statute must be complied with.

(b) By the common law, and by statute in some states, a corporation cannot adopt the same, or substantially the same, name as that of another corporation chartered by the same state.

34. A corporation may acquire a name by user or reputation, and it may thus be known by several names.

35. When a name has been given to a corporation in its creation, it cannot be changed without legislative authority.

¹²⁷ 156 Ill. 448, 41 N. E. 188.

¹²⁸ See, also, *People v. North River Sugar-Refining Co.*, 121 N. Y. 587, 24 N. E. 834; *Richardson v. Buhl*, 77 Mich. 632, 43 N. W. 1102; *State v. Standard Oil Co.*, 49 Ohio St. 137, 30 N. E. 279; *People v. Chicago Gas Trust Co.*, 130 Ill. 268, 22 N. E. 798; *State v. Nebraska Distilling Co.*, 29 Neb. 700, 46 N. W. 155.

As was stated in explaining the attributes of a corporate body, it is essential to the existence of such a body that it shall have some name by which it may be known and have succession, and under which it can contract and sue and be sued.¹²⁰

Ordinarily, in organizing a corporation, the incorporators may select any name they choose for the body, but in some states the choice is to some extent limited by statute. In Connecticut it was, and is perhaps still, required by statute that the name of every corporation organized under the general laws shall commence with the word, "The," and end with the word, "Company" or "Corporation"; and there are similar provisions in some of the other states.

Name of Another Corporation.

In some states it is expressly provided by statute that no corporation shall adopt the same name that is being used at the time by another corporation.¹²⁰ This, or a similar provision, it has been held, prevents the selection of a name that is substantially, though not exactly, the same as that of another corporation.¹²¹

¹²⁰ Ante, p. 17; *Conservators of the River Tone v. Ash*, 10 Barn. & C. 349, 1 Cumming, Cas. Priv. Corp. 23; *Mariot v. Mascal*, And. 206. "A corporation is a body politic, consisting of material bodies, which, joined together, must have a name to do things which concern the corporation, or else it is no corporation." *Conservators of the River Tone v. Ash*, supra. "The names of corporations are given of necessity, for the name is, as it were, the very being of the constitution; for, though it is the will of the king that erects them, yet the name is the knot of their combination, without which they could not perform their corporate acts; for it is nobody to plead and be impleaded, to take and give, until it hath gotten a name." 2 Bac. Abr. tit. "Corporations," c. 1. "The identity of name is the principal means for effecting that perpetuity of succession, with members frequently changing, which is an important purpose of incorporation." *Reg. v. Registrar*, 10 Q. B. 839.

¹²⁰ See *Elgin Butter Co. v. Elgin Creamery Co.*, 155 Ill. 127, 40 N. E. 616; *State v. McGrath*, 92 Mo. 355, 5 S. W. 29; *Illinois Watch Case Co. v. Pearson*, 140 Ill. 423, 31 N. E. 400.

¹²¹ Thus, it was held that, where there was a corporation by the name of "Kansas City Real-Estate and Stock Exchange," the secretary of state would not be compelled by a writ of mandamus to issue a certificate of incorporation to the "Kansas City Real-Estate Exchange." *State v. McGrath*, supra. The supreme court of Illinois, however, held that such a statute did not prevent the incorporation of the "Elgin Butter Company" and the "Elgin Creamery Company." *Elgin Butter Co. v. Elgin Creamery Co.*, supra.

At common law, and independently of any statute, a corporation has an exclusive right to the use of its name, and it will be protected by a court of equity, by injunction, against its use by another corporation. "The name of a corporation is a necessary element of its existence, and, aside from any statute, the right to its exclusive use will be protected upon the same principles that persons are protected in the use of trade-marks."¹⁸²

Acquisition by User and Reputation.

Generally, a name is given to a corporation when it is created, whether by a special law or under a general law. If this is not done, however, it may, in the absence of statutory regulations, acquire a name by user or by reputation;¹⁸³ and it has been held that it may thus be known by several names.¹⁸⁴

Change of Name.

Where a name has been given to a corporation in its creation, it cannot, unless authorized by statute, change its name, either directly, as by resolution, or indirectly, by the use of another.¹⁸⁵ Such a change must be made, if at all, under legislative authority, and the statute must be complied with.¹⁸⁶ Any act which provides that an existing corporation shall or may change its name, changes, in an essential particular, the organic law of such corporation, and is therefore an amendment of its charter, and subject to all the rules relating to amendments.¹⁸⁷ A change of its name does not change

¹⁸² *State v. McGrath*, 92 Mo. 355, 5 S. W. 29; *Newby v. Railway Co.*, Deady, 609, Fed. Cas. No. 10,144; *Holmes, Booth & Haydens v. Holmes, Booth & Atwood Manufg Co.*, 37 Conn. 278. See note to *R. W. Rogers Co. v. Wm. Rogers Manufg Co.*, 17 O. C. A. 579-591, 70 Fed. 1017.

¹⁸³ *Dutch West India Co. v. Van Moses*, 1 Strange, 612; *Anon.*, 3 Salk. 102; *Smith v. Plank-Road Co.*, 30 Ala. 650; *South School Dist. v. Blakeslee*, 13 Conn. 227; *Sykes v. People*, 132 Ill. 32, 23 N. E. 391.

¹⁸⁴ *Anon.*, 3 Salk. 102; *Minot v. Curtis*, 7 Mass. 441; *Society for Propagating the Gospel v. Young*, 2 N. H. 310.

¹⁸⁵ *Sykes v. People*, 132 Ill. 32, 23 N. E. 391; *Reg. v. Registrar*, 10 Q. B. 839.

¹⁸⁶ Such statutes have been enacted in some states. In New York the court is authorized to grant a corporation an order to change its name where it appears "that there is no reasonable objection." This leaves the question whether a change shall be allowed within the discretion of the court. In *re United States Mercantile Reporting & Collecting Agency*, 115 N. Y. 176, 21 N. E. 1034.

¹⁸⁷ *Sykes v. People*, 132 Ill. 32, 23 N. E. 391.

the identity of the corporation, or affect its title to property.¹³⁸ It is not in any sense the creation of a new corporation, and therefore the change may be authorized by a special act without violating the constitutional provision that corporations shall be created only under general laws.¹³⁹

Effect of Misnomer.

Misnomer of a corporation in a bond, note, or other deed or contract, does not vitiate it; but the corporation may sue or be sued thereon in its true name, with an allegation and proof that it is the party intended. Nor will a grant to or by a corporation be avoided because of a misnomer. And a devise or legacy to a corporation is good if the corporation is so described that it can be identified. In all of these cases parol evidence is admissible to explain the ambiguity and identify the corporation.¹⁴⁰

In legal proceedings, corporations must be correctly named. In a suit against a corporation, a misnomer not in substance is ground for plea in abatement; but if the corporation appears, and does not plead in abatement, it cannot afterwards object. If the misnomer is substantial, the proceedings will not affect the corporation. The same is true of criminal prosecutions against corporations. Misnomer is fatal to writs of execution, mandamus, etc., against a corporation. It is also fatal to a judgment against a corporation.¹⁴¹

RESIDENCE AND CITIZENSHIP OF CORPORATIONS.

36. A corporation has no legal existence beyond the boundaries of the state by which it was created. In so far as it can be a citizen or inhabitant, it is a citizen or inhabitant of that state, and of that state only, though it may do business in another.

¹³⁸ *Girard v. Philadelphia*, 7 Wall. 1.

¹³⁹ *Ante*, p. 44.

¹⁴⁰ *Hager's Town Turnpike Road Co. v. Creeger*, 5 Har. & J. (Md.) 122; *President, etc., of Berks & Dauphin Turnpike Road v. Myers*, 6 Serg. & R. 12; *Mount Palatine Academy v. Kleinschnitz*, 28 Ill. 133; *Medway Collar Manufactory v. Adams*, 10 Mass. 360; *Commercial Bank v. French*, 21 Pick. (Mass.) 486; *New York Institution for the Blind v. How's Ex'rs*, 10 N. Y. 84; *Society for Propagating the Gospel v. Young*, 2 N. H. 310; 1 *Thomp. Corp.* §§ 294, 295.

¹⁴¹ As sustaining these propositions, see *McGary v. People*, 45 N. Y. 155; *Glass v. Turnpike Co.*, 32 Ind. 376; 1 *Thomp. Corp.* §§ 290-293.

37. Where corporations are formed by corresponding legislation in different states,—as where corporations of different states are consolidated under similar acts in each state, or where one state makes a corporation of another state, as there conducted, a corporation of its own,—the legal effect is that there is a separate corporation in each state, which is a citizen of that state only.

38. An act merely recognizing a foreign corporation, and allowing it to do business in the state, is a mere license, and not a charter, and does not change the character of the body as a foreign corporation.

A corporation, as we have seen, has an individuality separate from that of the members who compose it. It acts and is regarded, for many purposes, as a distinct person, having many of the rights, and being subject to many of the liabilities, of natural persons. It is important, therefore, to determine the residence or citizenship of corporations. The question has generally arisen in connection with the question of jurisdiction of suits by and against corporations in the federal courts, but it may arise in many other ways.

It is well settled that, for the purpose of determining the jurisdiction of the federal courts of suits by and against corporations, a corporation "is to be regarded as if it were a citizen of the state where it was created, and no averment or proof of the citizenship of its members elsewhere will be permitted. There is a presumption of law which is conclusive."¹⁴² So it is, also, for other purposes.

¹⁴² *Baltimore & O. R. Co. v. Harris*, 12 Wall. 65, 1 Cumming, Cas. Priv. Corp. 46; *Ohio & M. R. Co. v. Wheeler*, 1 Black, 297; *Louisville, C. & C. R. Co. v. Letson*, 2 How. 497; *Shaw v. Mining Co.*, 145 U. S. 444, 12 Sup. Ct. 935, 2 Cumming, Cas. Priv. Corp. 5, *W. D. Smith, Cas. Corp.* 15, *Shep. Cas. Corp.* 55; note to *St. Louis, I. M. & S. Ry. Co. v. Newcom*, 6 C. C. A. 174, 56 Fed. 951. See *Bank of U. S. v. Deveaux*, 5 Cranch, 61; *Marshall v. Railroad Co.*, 16 How. 314, 327. For this reason it must appear somewhere (anywhere) in the pleadings, in an action against a corporation in a federal court, in what state it was created, if the only ground for federal jurisdiction is diverse citizenship. *Muller v. Dows*, 94 U. S. 444; *St. Louis, I. M. & S. Ry. Co. v. Newcom*, supra. An averment that a defendant corporation is a citizen of a certain state other than that in which suit is brought is not a sufficient allegation of diverse citizenship. The pleading

A "corporation, being a mere creature of a local law, can have no legal existence beyond the limits of the sovereignty where created."¹⁴³ This is none the less true because the corporation is allowed to do business in another state by the comity of the latter. This does not make it a citizen of the latter state for the purpose of federal jurisdiction, or for any other purpose.¹⁴⁴

The same principle applies where a statute uses the word "inhabitant" or "resident," and corporations are within the purpose of the law. A corporation cannot be an inhabitant of any state other than that by which it was created. Thus, under the act of congress

must show that it was created by the laws of a foreign state. *Lafayette Ins. Co. v. French*, 18 How. 404. The citizenship of a corporation, for the purposes of jurisdiction of a suit by or against it in the federal courts, is to be determined as of the time when the suit is commenced, and not as of the time when the cause of action accrued. *Stout v. Railroad Co.*, 8 Fed. 794, *Cumming, Cas. Priv. Corp.* 61. It was said by the supreme court of the United States that "a corporation itself can be a citizen of no state in the sense in which the word 'citizen' is used in the constitution of the United States. [See *Bank of U. S. v. Deveaux*, 5 Cranch, 61.] A suit may be brought in the federal courts by or against a corporation, but in such a case it is regarded as a suit brought by or against the stockholders of the corporation; and, for the purposes of jurisdiction, it is conclusively presumed that all the stockholders are citizens of the state which, by its laws, created the corporation." *Muller v. Dows*, *supra*. In this case it was clear that some of the stockholders of the corporation were not citizens of the state which created the corporation, for the corporation was an extensive railroad company, created by the laws of Iowa. Instead of basing the decision on a presumption which is evidently contrary to the fact, and instead of saying, what we have seen is not true in legal contemplation, that a suit by or against a corporation "is to be regarded as a suit by or against the stockholders of the corporation," it is better to recognize a corporation, as it is in the eye of the law in so far as suits by or against it are concerned, as having a personality distinct from that of its stockholders, and to say that the corporation itself is a citizen, for the purposes of federal jurisdiction, of the state by which it was created.

¹⁴³ *Paul v. Virginia*, 8 Wall. 168; *Bank v. Augusta v. Earle*, 13 Pet. 519; 585; *post*, p. 612.

¹⁴⁴ *Shaw v. Mining Co.*, 145 U. S. 444, 12 Sup. Ct. 935, 2 *Cumming, Cas. Priv. Corp.* 5. "A corporation created by and organized under the laws of a particular state, and having its principal office there, is, under the constitution and laws, for the purpose of suing and being sued, a citizen of that state. * * * By doing business away from their legal residence they do not change their citizenship, but simply extend the field of their operations. They reside at home, but do business abroad." *Baltimore & O. R. Co. v. Koontz*, 104 U. S. 5, 11, 12.

requiring suits in the federal courts, with certain exceptions, to be brought in the district whereof the defendant is an inhabitant, a corporation, for the purpose of suits against it in the federal courts, is an inhabitant of the state of its creation, and of that state only, though it may be doing business in other states, and may have an agent there, and may have submitted, in the other states, to the jurisdiction of their courts.¹⁴⁵

Charters from Several States.

It has been said that it is competent for several states to unite in creating the same corporation, or in consolidating several pre-existing corporations into a single one; but this is very inaccurate language. Several states may, by corresponding legislation, create several corporations, one in each state, having the same name, and the same object and powers, and being under the same management; but in the nature of things they cannot unite in creating the same corporation, for the laws of a state can have no extraterritorial effect. This is well settled, and seems so clear that it is strange that the question should ever have been controverted. Suppose, for instance, it is desired to incorporate a railroad company to construct and operate, under one management, a railroad through several states. In the absence of constitutional limitations, it is perfectly competent for the legislatures of these states to pass similar laws, chartering corporations to construct and operate the road, and to have the same name and the same powers in each state, and to be under one management, with principal offices in one state. So, where different corporations have been created by different states, it is competent for the legislatures of the different states to pass corresponding laws for the purpose of giving them the same name and putting them under one management, or, in popular understanding, of consolidating them. And where a corporation has been created by one state, it is competent for another state, by appropriate legis-

¹⁴⁵ Shaw v. Mining Co., 145 U. S. 444, 12 Sup. Ct. 935, 2 Cumming, Oas. Priv. Corp. 5, W. D. Smith, Cas. Corp. 15, Shep. Cas. Corp. 55; In re Keasby & Mattison Co., 16 Sup. Ct. 273; Day v. India-Rubber Co., Fed. Cas. No. 3,685; Donnelly v. Cordage Co., 66 Fed. 613; Gorham Manuf'g Co. v. Watson, 74 Fed. 418; Miller v. Manufacturing Co., 46 Fed. 882; post, pp. 612, 637.

lation, to make that corporation, as chartered and conducted in the first-named state, a corporation of its own.¹⁴⁶

In none of these cases, however, do the different states unite in creating the same corporation, or in consolidating the several corporations into a single one. The result of such legislation is to create a separate and distinct corporation in each state. The corporations may have the same name in each state, it is true, and they may have the same powers, and be under one management, so that for all practical purposes they are conducted as a single corporation; but in law they are separate and distinct corporate bodies. The reason is that it is not possible for a state to pass a law which will have effect in another state, and a law of one state, therefore, cannot create, nor aid in creating, a corporation in another state.¹⁴⁷

¹⁴⁶ "It is entirely competent for the state, by its legislation, to determine the mode of creating corporations within its limits; and if it sees fit to declare that a foreign corporation may become a corporation of the state by building a railroad therein, and filing a copy of its articles of incorporation with the secretary of state, I have no doubt that compliance with these terms constitutes the foreign corporation a domestic corporation with respect to all its transactions within such state." *Stout v. Railroad Co.*, 8 Fed. 794, 1 Cumming, Cas. Priv. Corp. 61. And see *Baltimore & O. R. Co. v. Gallahue's Adm'rs*, 12 Grat. (Va.) 655; *Louisville Trust Co. v. Louisville, N. A. & O. R. Co.*, 75 Fed. 433.

¹⁴⁷ *Ohio & M. R. Co. v. Wheeler*, 1 Black, 286; *Missouri Pac. Ry. Co. v. Meeh*, 69 Fed. 753, 16 C. O. A. 510; *Railway Co. v. Whitton's Adm'r*, 13 Wall. 270; *Newport & C. Bridge Co. v. Woolley*, 78 Ky. 523; *Fitzgerald v. Missouri Pac. Ry. Co.*, 45 Fed. 812; *Muller v. Dows*, 94 U. S. 444, 1 Cumming, Cas. Priv. Corp. 53; *Nashua & L. R. Corp. v. Boston & L. R. Corp.*, 136 U. S. 356, 10 Sup. Ct. 1004; *Chicago & N. W. R. Co. v. Auditor*, 53 Mich. 91, 18 N. W. 586; *Racine & M. R. Co. v. Farmers' Loan & Trust Co.*, 49 Ill. 331; *Rece v. Newport News & M. V. Co.*, 32 W. Va. 164, 9 S. E. 212; *Bishop v. Brainerd*, 28 Conn. 289. In *Missouri Pac. Ry. Co. v. Meeh*, *supra*, it was said: "At this day it must be regarded as settled beyond doubt or controversy that two states of this Union cannot by their joint action create a corporation which will be regarded as a single corporate entity, and, for jurisdictional purposes, a citizen of each state which joined in creating it. One state may create a corporation of a given name, and the legislature of an adjoining state may declare that the same legal entity shall be or become a corporation of that state as well, and be entitled to exercise within its borders, by the same board of directors and officers, all of its corporate functions. Nevertheless, the result of such legislation is not to create a single corporation, but two corporations of the same name, having a different paternity." In *Chicago & N. W. R. Co. v. Auditor*, *supra*, Judge Cooley said: "It is impossible to conceive of one joint act performed simultaneously by two

In the leading case of *Ohio & M. R. Co. v. Wheeler*,¹⁴⁸ the plaintiff described itself as a corporation created and existing under the laws of the states of Indiana and Ohio, having its principal office in Cincinnati, Ohio. It sued Wheeler in the circuit court of the United States for the district of Indiana, describing him as a citizen of Indiana. The supreme court of the United States held that there was no jurisdiction, on the ground of diverse citizenship. "It is true," it was said, "that a corporation by the name and style of the plaintiff appears to have been chartered by the states of Indiana and Ohio, clothed with the same capacities and powers, and intended to accomplish the same objects; and it is spoken of in the laws of the states as one corporate body, exercising the same powers and fulfilling the same duties in both states. Yet it has no legal existence in either state, except by the law of the state; and neither state could confer on it a corporate existence in the other, nor add to or diminish the powers to be there exercised. It may, indeed, be composed of and represent, under the corporate name, the same natural persons; but the legal entity or person, which exists by force of law, can have no existence beyond the limits of the state or sovereignty which brings it into life, and indues it with its faculties and powers. The President and Directors of the Ohio & Mississippi Railroad Company is, therefore, a distinct and separate corporate body in Indiana from the corporate body of the same name in Ohio, and they cannot be joined in a suit as one and the same plaintiff, nor maintain a suit in that character against a citizen of Ohio or Indiana in a circuit court of the United States." As was said by

sovereign states, which shall bring a single corporation into being, except it be by compact or treaty. There may be separate consent given for the consolidation of corporations separately created; but, when the two unite, they severally bring to the new entity the powers and privileges already possessed, and the consolidated company simply exercises in each jurisdiction the powers the corporation there chartered had possessed, and succeeds there to its privileges." In *Quincy Railroad Bridge Co. v. Adams Co.*, 88 Ill. 615, 619, it is said: Two states "have no power to unite in passing any legislative act. It is impossible, in the very nature of their organizations, that they can do so. They cannot so fuse themselves into a single sovereignty, and, as such, create a body politic which shall be a corporation of the two states, without being a corporation of each state or of either state."

¹⁴⁸ 1 Black, 286.

the Illinois court, "the only possible status of a company acting under charters from two states is that it is an association incorporated in and by each of the states; and, when acting as a corporation in either of the states, it acts under the authority of the charter of the state in which it is then acting, and that only, the legislation of the other state having no operation beyond its territorial limits."¹⁴⁹ Whenever one state makes a corporation of another state, as there constituted and conducted, a corporation of its own quoad hoc any property or transactions within its territorial jurisdiction, the corporation, in so far as suits in the federal courts in that state and transactions there are concerned, is to be regarded as a citizen of that state only, and cannot be regarded as a citizen of both states.¹⁵⁰

Charter Distinguished from License.

Acts of the legislature creating corporations must be distinguished from acts which merely recognize a corporation chartered by another state, and allow it to do business within the state on compliance with certain conditions. This distinction is illustrated by the case of *Baltimore & O. R. Co. v. Harris*.¹⁵¹ The Baltimore & Ohio Railroad Company had been incorporated by an act of the legislature of Maryland. Afterwards the legislature of Virginia passed an act whereby, after reciting the Maryland act, it was declared "that the same rights and privileges shall be, and are hereby, granted to the aforesaid company within the territory of Virginia, and the said company shall be subject to the same pains, penalties, and obligations as are imposed by said act; and the same rights, privileges, and immunities which are reserved to the state of Maryland or to the citizens thereof are hereby reserved to the state of Virginia and her citizens." It was held in this case that the Virginia act was a mere license, and nothing more, and that the license was given to the Maryland corporation as such, and in no degree changed the character or status of that body; that it remained a Maryland corporation only, and therefore a Maryland citizen only for the purposes of federal jurisdiction.¹⁵²

¹⁴⁹ *Quincy Railroad Bridge Co. v. Adams Co.*, 88 Ill. 615, 619.

¹⁵⁰ *Stout v. Sioux City & P. R. Co.*, 8 Fed. 794, 1 Cumming, Cas. Priv. Corp. 61.

¹⁵¹ 12 Wall. 65, 1 Cumming, Cas. Priv. Corp. 46.

¹⁵² And see *Pennsylvania R. Co. v. St. Louis, A. & T. H. R. Co.*, 118 U. S.

EXTENSION OF CHARTER—CREATION OF NEW CORPORATION.

39. It is competent for the legislature to extend a charter before it has expired, or to revive a charter after its expiration. An act extending the period of existence of a corporation beyond the time for which it was originally created, even under a new name, does not create a new corporation. If, however, a new corporation is intended to be created, though with the same name and the same members, the old and the new body are distinct corporations.

The legislature, subject to constitutional limitations, may not only pass an act before the charter of a corporation expires, extending the same,¹⁵³ but it may pass an act reviving a charter which has already expired, so as to revive the former corporation in all its original force, and not create a new one.¹⁵⁴ It is sometimes difficult to distinguish between an act creating a new corporation, with the same name and the same members as those of a former or an existing corporation, and an act which merely continues the existence of a corporation previously created. The distinction is important. For instance, if a statute grants special privileges to corporations thereafter incorporated, they cannot be claimed by a corporation previously created, though its charter may be afterwards extended.¹⁵⁵ Again, if a new corporation is created, though with the same name and the same members as those of an existing corporation, whose charter is about to expire, the new corporation is not liable for the debts of the old, while it is otherwise if the existence of the old corporation is merely extended.¹⁵⁶

290, 6 Sup. Ct. 1094; *Morgan v. Railroad Co.*, 48 Fed. 705; note to *St. Louis, I. M. & S. Ry. Co. v. Newcom*, 6 C. C. A. 174, 175. Cf. *Louisville Trust Co. v. Louisville, N. A. & O. R. Co.*, 75 Fed. 433.

¹⁵³ *Foster v. Essex Bank*, 16 Mass. 245, 1 Cumming, Cas. Priv. Corp. 464.

¹⁵⁴ *President, etc., of Lincoln & K. Bank v. Richardson*, 1 Greenl. (Me.) 79; *President & Selectmen of Port Gibson v. Moore*, 13 Smedes & M. (Miss.) 157.

¹⁵⁵ *Frostburg Min. Co. v. Cumberland & P. R. Co.*, 81 Md. 28, 31 Atl. 698.

¹⁵⁶ *Bellows v. Bank*, 2 Mason, 31, Fed. Cas. No. 1,279.

A mere change of name, as we have seen, does not create a new corporate body.¹⁵⁷ "To ascertain whether a charter creates a new corporation or merely continues the existence of the old one, we must look to its terms, and give them a construction consistent with the legislative intent and the intent of the corporators."¹⁵⁸ In a late Maryland case the act under consideration was entitled "An act to extend an act entitled 'An act to incorporate the Wither's Mining Company,' passed at the December session, 1847, chapt. 306"; and it provided that said act, and a subsequent act amending it, "be and the same are hereby continued in full force and effect" for 30 years, and declared, after giving the company a new name, "that the company by such name shall succeed to all the rights, powers, liabilities, and obligations" of the company as previously named. It was held that this did not create a new corporation, but merely continued the existence of the old one.¹⁵⁹ On the other hand, where a bank was created as a corporation, with the same name as that of an old bank, whose charter was about to expire, and the statutes and circumstances together showed that the legislature did not intend merely to continue the existing corporation, it was held that there was a new and distinct corporation, though most of the stockholders were the same, and that the new bank, therefore, was not liable for the debts of the old bank.¹⁶⁰

40. PROOF OF CORPORATE EXISTENCE.

The sufficiency of the proof of corporate existence will depend to a great extent upon the nature of the proceeding in which the question is raised, and the circumstances of the particular case. In quo warranto proceedings by the state to test the right of an alleged corporation to exercise corporate powers, corporate existence *de jure* must be shown; and to show this it must be made to appear that there is a valid law creating or authorizing such a corporation, that

¹⁵⁷ Ante, p. 74.

¹⁵⁸ Per Mr. Justice Story, in *Bellows v. Bank*, *supra*.

¹⁵⁹ *Frostburg Min. Co. v. Cumberland & P. R. Co.*, *supra*.

¹⁶⁰ *Bellows v. Bank*, *supra*. And see *President & Selectmen of Port Gibson v. Moore*, 13 *Smedes & M. (Miss.)* 157.

there was a valid organization under it, and a substantial compliance with all conditions precedent.¹⁶¹

On the other hand, as has heretofore been stated, and as will presently be shown at some length, if the question of corporate existence is raised collaterally, it is sufficient if a de facto existence be shown.¹⁶² Such proof is admissible whenever the question comes up collaterally, as in a criminal prosecution for larceny, forgery, or any other crime against an alleged corporation;¹⁶³ or in any civil proceeding, other than proceedings by the state to test the existence of the alleged corporation,¹⁶⁴ except, in some states, proceedings by the corporation to condemn land under the power of eminent domain.¹⁶⁵ As will be seen, by the weight of authority, it is only necessary, in order to prove de facto corporate existence, to show a valid law under which the alleged corporation might have been formed, a colorable bona fide compliance with that law, and an assumption of corporate powers, or user.¹⁶⁶

Again, as we shall see, there are many cases in which a party may, by his conduct, as by dealing with or holding out a body as a corporation, be estopped to deny its existence as a corporate body.¹⁶⁷ Here, by the weight of authority, it is not necessary to prove even a de facto corporate existence. All that is necessary is to show the facts that will operate as an estoppel.¹⁶⁸ Where a person has contracted or dealt with an association as a corporation, proof of that fact alone is prima facie evidence of the corporate existence of the body as against him, as in an action by the alleged corporation on a subscription to its stock.¹⁶⁹

The mode of proving acts of the legislature is a question of the general law of evidence. There is no difference between the mode of proving the charter of a corporation and the mode of proving other

¹⁶¹ Ante, p. 55; post, p. 86.

¹⁶² Post, p. 86.

¹⁶³ *Calkins v. State*, 18 Ohio St. 370; *State v. Habib*, 18 R. I. 558, 30 Atl. 462.

¹⁶⁴ 1 Mor. Corp. § 37.

¹⁶⁵ Post, p. 88.

¹⁶⁶ Post, p. 86; *Bon Aqua Imp. Co. v. Standard Fire Ins. Co.*, 34 W. Va. 764, 12 S. E. 771.

¹⁶⁷ Post, p. 89.

¹⁶⁸ Post, p. 105.

¹⁶⁹ *United States Vinegar Co. v. Schlegel*, 143 N. Y. 587, 38 N. E. 729.

legislative acts. A charter granted by a public statute need not be proved at all, for the courts must take judicial notice of all public acts.¹⁷⁰ Private acts, however, must be proved, for the courts do not take judicial notice of them.¹⁷¹ For the mode of proving statutes, the reader must refer to works on evidence. Foreign laws, including charters granted by another state, must be proved.¹⁷²

We have seen that acceptance of a charter by the corporators may, unless a particular mode of acceptance is prescribed by the legislature, be shown by proof of any act on the part of the corporators which shows an unequivocal intention to accept, as by showing that they organized and exercised corporate powers. If such acts are shown, acceptance will be presumed.¹⁷³ Unless there is statutory requirement of other evidence, the organization of a corporation and user, for the purpose of showing a de facto existence, may be shown by parol evidence.¹⁷⁴ It has been said that general reputation of corporate existence is sufficient,¹⁷⁵ but this dictum cannot be supported by authority. There must be evidence, not only of an act authorizing incorporation and user of corporate powers, but also of organization in at least colorable compliance with the act.¹⁷⁶ The records, books, and minutes of a corporation, embracing the proceedings in its organization under its charter, or under the general law, when regular and identified by the person authorized to make them, are prima facie evidence of the organization of the corporation.¹⁷⁷ When it is shown that there was an act authorizing the

¹⁷⁰ *Hays v. Bank*, 9 Grat. (Va.) 127; *Bank of Utica v. Meagher*, 18 Johns. (N. Y.) 341; *Williams v. Bank*, 2 Humph. (Tenn.) 339; *Stribbling v. Bank*, 5 Rand. (Va.) 132; *White Water Valley Canal Co. v. Boden*, 8 Blackf. (Ind.) 130.

¹⁷¹ 1 Mor. Corp. § 38; *Ohio & I. R. Co. v. Ridge*, 5 Blackf. (Ind.) 78; *State v. Trustees of Vincennes University*, 5 Ind. 77, 87, 91; *Bailey v. Trustees of Lincoln Academy*, 12 Mo. 174.

¹⁷² 1 Mor. Corp. § 39, *United States Bank v. Stearns*, 15 Wend. (N. Y.) 314.

¹⁷³ Ante, p. 53; *Bank of Manchester v. Allen*, 11 Vt. 302.

¹⁷⁴ *Calkins v. State*, 18 Ohio St. 370; *State v. Habib*, 18 R. I. 558, 30 Atl. 462; *Yakima Nat. Bank v. Knipe*, 6 Wash. 348, 33 Pac. 834.

¹⁷⁵ *Fleener v. State*, 58 Ark. 98, 23 S. W. 1.

¹⁷⁶ *State v. Murphy*, 17 R. I. 698, 24 Atl. 473; *Porter v. State*, 141 Ind. 483, 40 N. E. 1061; *Owen v. Shepard*, 8 O. C. A. 244, 59 Fed. 746.

¹⁷⁷ *Buncombe Turnpike Co. v. McCarron*, 1 Dev. & B. (N. C.) 306; *Coffin v. Collins*, 17 Me. 440; *Glenn v. Orr*, 96 N. C. 413, 2 S. E. 538; *Semple v. Glenn*,

formation of an alleged corporation, that it was formed under the act, and has since acted as a corporation, compliance with particular provisions of the act will be presumed, in the absence of evidence to the contrary.¹⁷⁸

In many states it is expressly provided by statute that a certified copy of the certificate or letters of incorporation or articles of association, filed with the secretary of state or other officer (the statutes necessarily varying in the different states), shall be prima facie evidence of corporate existence.¹⁷⁹ This, however, does not exclude other competent evidence of incorporation, unless it is expressly so provided.¹⁸⁰ In some states it is provided that, whenever it is necessary to prove the incorporation of a company, evidence that it is doing business under a certain name shall be prima facie evidence of its due incorporation.¹⁸¹

If the certificate of incorporation and record thereof have been lost or destroyed, parol evidence is admissible to show compliance with the law in the organization of the company, and to prove the contents of the certificate; and it is not necessary that such evidence should be so minute as to permit of the reproduction of the certificate in all its details. It is sufficient if it is so full as to show that the law was complied with.¹⁸² Long acquiescence by the public in the exercise of the franchise in such a case raises a presumption of organization in conformity to law, in aid of the parol evidence.¹⁸³

91 Ala. 245, 9 South. 265; *Peake v. Railroad Co.*, 18 Ill. 88. If the acceptance of a charter is recorded on the books, they are the best evidence; and parol evidence is admissible only under the rules allowing secondary evidence. *Coffin v. Collins*, supra; *Hudson v. Carman*, 41 Me. 84. It must be made to appear that the books offered in evidence are the corporation books; that they have been kept as such; and that the entries have been made by an authorized person. *President, etc., of the Highland Turnpike Co. v. M'Kean*, 10 Johns. (N. Y.) 154.

¹⁷⁸ *Bank of U. S. v. Lyman*, 1 Blatchf. 297, Fed. Cas. No. 924.

¹⁷⁹ *Marshall v. Bank*, 108 N. C. 639, 13 S. E. 182.

¹⁸⁰ *Edelhoff v. State* (Wyo.) 38 Pac. 627.

¹⁸¹ *Canal Street Gravel-Road Co. v. Paas*, 95 Mich. 372, 54 N. W. 907.

¹⁸² *Rose Hill & E. R. Co. v. People*, 115 Ill. 133, 3 N. E. 725.

¹⁸³ *Rose Hill & E. R. Co. v. People*, supra.

CHAPTER III.

EFFECT OF IRREGULAR INCORPORATION.

41-42. Corporations De Facto.

43-44. Estoppel to Deny Corporate Existence.

45. Liability of Associates as Partners.

CORPORATIONS DE FACTO.

41. Where persons attempt, in good faith, to organize a corporation under a statute that is valid, and that authorizes such a corporation, and afterwards assume to exercise corporate powers, there is a corporation de facto, though, by reason of failure to comply with the statute, there may not be a corporation de jure; and the corporate character of the association can only be questioned by the state in a direct proceeding brought for that purpose. By the weight of authority, to constitute a corporation de facto within this rule, there must be
- (a) A valid law, and one which authorizes such a corporation.
 - (b) An attempt in good faith to organize under the statute.
 - (c) At least a colorable or apparent compliance with the statute.
 - (d) An assumption of corporate powers.
42. The doctrine concerning de facto corporations is based on grounds of public policy, and does not depend on any element of estoppel.

A corporation may exist in fact without being legally constituted. Such a corporation is called a corporation de facto, as distinguished from a corporation de jure. "This phrase [de facto] is used to characterize an officer, a government, a past action, or a state of affairs which exists actually and must be accepted for all practical pur-

poses, but which is illegal or illegitimate. In this sense it is the contrary of 'de jure.'"¹ The term "de facto," as applied to a corporation, means a body which actually exists, for all practical purposes, as a corporate body, but which, because of failure to comply with some provision of the law, has no legal right to corporate existence as against the state. A corporation de jure, on the other hand, is a corporation in law as well as in fact. Not even the state can deprive it of its corporate existence in violation of the terms of its charter.

The distinction between a corporation de jure and a corporation de facto is very important. A corporation de jure has a right to corporate existence even as against the state. The state cannot, even by a direct proceeding, deprive it of this right, contrary to the terms of its charter. A corporation de facto has a corporate existence, even as against the state, where the state attacks its right collaterally; and it has such right as against private individuals, whether they attack its corporate existence collaterally or directly. The state, which alone has the power to incorporate, may waive irregularities in the organization of corporations; and, so long as the state remains inactive in the premises, individuals must acquiesce.² "Where the law authorizes a corporation, and there is an effort, in good faith, to organize a corporation under the law, and thereupon, as a result of such effort, corporate functions are assumed and exercised, the organization becomes a corporation de facto, and, as a general rule, the legal existence of such a corporation cannot be inquired into collaterally, although some of the required legal formalities may not have been complied with. Ordinarily, such an inquiry can only be made in a direct proceeding brought in the name of the state."³

A corporation de facto, that by regularity of organization might be one de jure, can make contracts, purchase, hold, and convey property, and sue and be sued, in the same manner as if it were a corporation de jure, for no one can object but the state. "A corporation de facto may legally do and perform every act and thing which the

¹ Black, Law Dict. tit. "De Facto."

² North v. State, 107 Ind. 356, 8 N. E. 159, and cases cited in the following notes.

³ Hasselman v. Mortgage Co., 97 Ind. 365.

same entity could do and perform were it a *de jure* corporation. As to all the world except the paramount authority under which it acts, and from which it receives its charter, it occupies the same position as though in all respects valid; and even as against the state, except in direct proceedings to arrest its usurpation of power, it is submitted, its acts are to be treated as efficacious." ⁴ "Mere irregularities in organization cannot be shown collaterally, where there is no defect of power." ⁵ The doctrine is not limited in its application to domestic corporations, but extends to foreign corporations as well.⁶

Some of the courts have held that the doctrine of *de facto* corporations does not apply to a case in which an alleged corporation attempts to exercise the power of eminent domain by the appropriation of private property to public use; that in such a proceeding, if

⁴ *People v. La Rue*, 67 Cal. 530, 8 Pac. 84. And see *Heaston v. Railroad Co.*, 16 Ind. 275, 1 Cumming, Cas. Priv. Corp. 417, W. D. Smith, Cas. Corp. 20, and *Shep. Cas. Corp.* 134; *Williamson v. Association*, 89 Ind. 389; *Pinnegan v. Noerenberg*, 52 Minn. 239, 53 N. W. 1150; *Eaton v. Aspinwall*, 19 N. Y. 119; *Buffalo & A. R. Co. v. Cary*, 26 N. Y. 75, 1 Cumming Cas. Priv. Corp. 411; *Lamming v. Galusha*, 81 Hun, 247, 30 N. Y. Supp. 767; *Thompson v. Candor*, 60 Ill. 244; *People v. Board*, 111 Ill. 171; *Hudson v. Green Hill Seminary Corp.*, 113 Ill. 618; *Bushnell v. Machine Co.*, 138 Ill. 67, 27 N. E. 596; *Duggan v. Investment Co.*, 11 Colo. 113, 17 Pac. 105; *Appleton Mut. Fire Ins. Co. v. Jesser*, 5 Allen (Mass.) 446; *Butchers' & D. Bank v. McDonald*, 130 Mass. 264, 1 Cumming, Cas. Priv. Corp. 420; *Cochran v. Arnold*, 58 Pa. St. 399; *Searsburgh Turnpike Co. v. Cutler*, 6 Vt. 315; *East Norway Lake Church v. Froislie*, 37 Minn. 447, 35 N. W. 260; *Stout v. Zulick*, 48 N. J. Law, 599, 7 Atl. 362; *McTighe v. Construction Co.*, 94 Ga. 306, 21 S. E. 701; *Whitney v. Robinson*, 53 Wis. 309, 10 N. W. 512; *Selma & T. R. Co. v. Tipton*, 5 Ala. 787; *Dannebrog Min. Co. v. Allment*, 26 Cal. 286; *Dean v. Davis*, 51 Cal. 406; *Bakersfield Town Hall Ass'n v. Chester*, 55 Cal. 98; *Pape v. Bank*, 20 Kan. 440; *Chicago K. & W. R. Co. v. Stafford Co. Com'rs*, 36 Kan. 121, 12 Pac. 593; *Upton v. Hansbrough*, 3 Biss. 417, Fed. Cas. No. 16,801. "The reason is that, if rights and franchises have been usurped, they are the rights and franchises of the sovereign, and he alone can interpose. Until such interposition, the public may treat those possessing and exercising corporate powers under color of law as doing so rightfully. The rule is in the interest of the public, and is essential to the safety of business transactions with corporations." *Duggan v. Investment Co.*, 11 Colo. 113, 17 Pac. 105.

⁵ *Heaston v. Railroad Co.*, *supra*.

⁶ *Bank of Toledo v. International Bank*, 21 N. Y. 542; *Lancaster v. Improvement Co.*, 140 N. Y. 576, 35 N. E. 964; *Wright v. Lee*, 4 S. D. 237, 55 N. W. 931; *post*, p. 632.

the question is raised, it must show that it is a corporation de jure.⁷ Other courts make no such distinction, but apply the doctrine in condemnation proceedings as well as in other cases.⁸

If a pretended corporation is neither a corporation de jure nor one de facto, it has no standing whatever, and its corporate existence may be questioned collaterally, and by a private individual as well as by the state,⁹ provided there is no element of estoppel.¹⁰

By the better opinion, though there are decisions to the contrary, after the period of existence of a corporation has expired by force of express provision in its charter or in a general law, it is not even a corporation de facto. By the expiration of its charter it becomes ipso facto dissolved, and no longer has any existence at all.¹¹ It follows that its existence after that time can be questioned by any person who has not estopped himself, and collaterally as well as directly. Thus, if a pretended corporation, after expiration of its charter, assumes to execute a conveyance, and the grantee, or one claiming under him, sues a third person, who holds adversely, to recover possession, the latter may question the validity of the conveyance, and dispute the existence of the corporation.¹²

The doctrine concerning de facto corporations does not prevent a collateral attack on the right of a corporation to exercise a franchise separate and distinct from the franchise of being a corporation. It has been held, for instance, that, even conceding that the right of an association to exist as a corporation after the expiration of the time limited in its charter cannot be questioned by a private

⁷ *Atlantic & O. R. Co. v. Sullivant*, 5 Ohio St. 276; *Atkinson v. Railroad Co.*, 15 Ohio St. 21.

⁸ *Reisner v. Strong*, 24 Kan. 410; *McAuley v. Railway Co.*, 83 Ill. 348; *Ward v. Railroad Co.*, 119 Ill. 287, 10 N. E. 365; *Wellington & P. R. Co. v. Cashie & C. R. & L. Co.*, 114 N. C. 690, 19 S. E. 646.

⁹ *Martin v. Deetz*, 102 Cal. 55, 36 Pac. 368; *Childs v. Hurd*, 32 W. Va. 66, 9 S. E. 362.

¹⁰ *Post*, p. 99.

¹¹ *Bradley v. Reppell* (Mo. Sup.) 32 S. W. 645. And see *Grand Rapids Bridge Co. v. Prange*, 35 Mich. 400; *Sturges v. Vanderbilt*, 73 N. Y. 384; *Dobson v. Simonton*, 86 N. C. 492; *Krutz v. Town Co.*, 20 Kan. 397. Contra, *Bushnell v. Machine Co.*, 138 Ill. 67, 27 N. E. 596; *Miller v. Newburg Orrel Coal Co.*, 81 W. Va. 836, 8 S. E. 600. See *post*, p. 232.

¹² *Bradley v. Reppell*, *supra*.

individual in a collateral proceeding, he can thus question the right of a corporation to take tolls after the expiration of the period during which it was authorized to take tolls, as he does not thereby question its corporate existence.¹³

What is Necessary to Constitute a Corporation De Facto.

Having once determined that a particular association is a corporation de facto, there is little difficulty in applying the principles of law as stated above. But there is much confusion and direct conflict in the decisions as to what constitutes a corporation de facto, as distinguished from an association which pretends to be a corporation, but which has no existence at all as such, either de jure or de facto. And the books do not throw as much light on the question as might be expected.¹⁴

Most of the courts hold that there is a corporation de facto whenever there is a valid law under which a particular kind of corporation may lawfully be organized, and persons having the required qualifications undertake, in good faith, to organize such a corporation thereunder, comply at least colorably with the law, and afterwards assume to act as a corporation, though particular provisions of the law are not complied with. And they hold that it is altogether immaterial, in such a case, whether compliance with the particular provisions was intended by the legislature as a condition precedent to the formation of the corporation or not. Thus, an

¹³ *Grand Rapids Bridge Co. v. Prange*, 35 Mich. 400.

¹⁴ The state of the authorities on this subject is thus described by Judge Thompson in his late work on Corporations: "It is impossible to formulate a rule on the subject of de facto corporations, which will be applicable in all American jurisdictions, or which will receive uniform support from the decisions in any one such jurisdiction. Those decisions oscillate between two extreme views: (1) That where a body of men act as a corporation, and in the ostensible possession of corporate powers, it will be conclusively presumed, in all cases except in a direct proceeding against them by the state to vacate their franchises, that they are a corporation. (2) That the conditions named in statutes authorizing the organization of corporations are conditions precedent, and must be strictly complied with, or the corporation does not exist; and that the want of compliance with any one condition precedent may be shown by any one, in a private litigation with the pretended corporation, unless he has estopped himself by his conduct from challenging its corporate existence, and frequently without reference to the question of estoppel." 1 *Thomp. Corp.* § 495.

association has been held a corporation de facto, though there was not sufficient notice of the meetings held for the purpose of organizing, and though the certificates of incorporation were not properly executed, acknowledged, or recorded, as required by the statute.¹⁵ And there are many other cases to the same effect, or apparently so.¹⁶ All that is necessary, according to this doctrine, is that there shall be a law under which such a corporation as the one in question might have been formed, that there shall have been a bona fide attempt to organize, and a colorable compliance with the provisions of the law, and that there shall have been an assumption of corporate powers, or "user," as it is termed. "Where it is shown that there is a charter or law under which a corporation, with the powers assumed, might lawfully be incorporated, and there is a colorable compliance with the requirements of the charter or law, and a user of the rights claimed under the charter or law, the existence of a corporation de facto is established."¹⁷ "Two things are necessary to be shown to establish a corporation de facto, viz.: (1) The existence of a charter or some law under which a corporation, with the powers assumed, might lawfully be created; and (2) a user by the party to the suit of the rights claimed to be conferred by such charter or law. If the law exists, and the record exhibits a bona fide attempt to organize under it, very slight evidence of user beyond this is all that can be required."¹⁸

¹⁵ *East Norway Lake Church v. Froislie*, 37 Minn. 447, 35 N. W. 260.

¹⁶ See *Attorney General v. Stevens*, 1 N. J. Eq. 369; *Stout v. Zulick*, 48 N. J. Law, 599, 7 Atl. 362; *Eaton v. Walker*, 76 Mich. 579, 43 N. W. 638; *Methodist Church v. Pickett*, 19 N. Y. 482, 1 Cumming, Cas. Priv. Corp. 407; *Society Perun v. Cleveland*, 43 Ohio St. 481, 3 N. E. 357; *Finnegan v. Noerenberg*, 52 Minn. 239, 53 N. W. 1150; *Williamson v. Association*, 89 Ind. 389; *Hasselman v. Mortgage Co.*, 97 Ind. 365; *North v. State*, 107 Ind. 356, 8 N. E. 159; *Cochran v. Arnold*, 58 Pa. St. 399; *Thompson v. Candor*, 60 Ill. 244; *Hudson v. Green Hill Seminary Corp.*, 113 Ill. 618; *Bushnell v. Machine Co.*, 138 Ill. 67, 27 N. E. 596; *Miami Powder Co. v. Hotchkiss*, 17 Ill. App. 622; *Merriman v. Magiveny*, 12 Heisk. (Tenn.) 494; *Pape v. Bank*, 20 Kan. 440; *Haas v. Bank*, 41 Neb. 754, 60 N. W. 85; *Humphreys v. Mooney*, 5 Colo. 282; *Jones v. Hardware Co.*, 21 Colo. 263, 40 Pac. 457.

¹⁷ *Stout v. Zulick*, *supra*.

¹⁸ *Eaton v. Walker*, *supra*. It will be noticed that, while the court here says that two things only are necessary to constitute a de facto corporation, namely, the law authorizing incorporation, and user under that law, it proceeds at once

Same—Necessity for Valid Law Authorizing Incorporation.

In the first place, by the weight of authority, it is always essential to the existence of a corporation de facto that there shall be some law under which such a corporation might have been legally created or organized. If there is no law at all authorizing the formation of such a corporation, there can be no corporation de facto, even though there may have been an assumption of corporate powers. In a Wisconsin case there had been an attempt to organize two churches into one corporate body, whereas the statute only authorized a corporation composed of one church. It was held that the association was not even a corporation de facto. "To be a corporation de facto," it was said, "it must be possible to be a corporation de jure; and acts done in the former case must be legally authorized to be done in the latter, or they are not protected or sanctioned by the law. Such acts must have an apparent right."¹⁹ Within this rule, an unconstitutional law must be regarded as the same as no law at all.²⁰ There are a few cases which hold that a de facto corporation may exist under an unconstitutional act,²¹ but it is difficult to see how they can be supported, when we consider

to specify a third essential; that is, "a bona fide attempt to organize" under the law. And it is clear that all three of these things are necessary. See *Finnegan v. Noerenberg*, 52 Minn. 239, 53 N. W. 1150. "A corporation de facto," said the Colorado court, "presupposes a charter or a law authorizing the creation of such a corporation; that there has been an attempt in good faith to comply with its provisions; and that there has been user or the exercise of corporate powers under it." *Duggan v. Investment Co.*, 11 Colo. 113, 17 Pac. 105.

¹⁹ *Evenson v. Ellingson*, 67 Wis. 634, 31 N. W. 342. And see *Abbott v. Refining Co.*, 4 Neb. 416; *State v. Critchett*, 37 Minn. 13, 32 N. W. 787; *Duke v. Taylor* (Fla.) 19 South. 172; *American Loan & Trust Co. v. Minnesota & N. W. R. Co.*, 157 Ill. 641, 42 N. E. 153.

²⁰ *Eaton v. Walker*, 76 Mich. 579, 43 N. W. 638; *Burton v. Schildbach*, 45 Mich. 504, 8 N. W. 497; *Green v. Graves*, 1 Doug. (Mich.) 351; *Brandenstein v. Hoke*, 101 Cal. 131, 35 Pac. 562. In *McTighe v. Macon Const. Co.*, 94 Ga. 306, 21 S. E. 701, it was held, after a review of the cases, and a consideration of the reasons on which the doctrine of de facto corporations is based, that a corporation attempted to be created by a special act, which is unconstitutional, may, nevertheless, exist as a de facto corporation, if there is a general law under which it might have been incorporated.

²¹ *Coxe v. State*, 144 N. Y. 396, 39 N. E. 400. And see the dictum in *Winget v. Association*, 128 Ill. 67, 21 N. E. 12.

that "an unconstitutional act is not a law. It confers no rights. It imposes no duties. It affords no protection. It creates no office. It is, in legal contemplation, as inoperative as if it had never been passed."²² As we have seen, after the period of existence of a corporation has expired by express limitation in its charter or in a general law, it is not a corporation de facto. There is no law under which it can exist.²³

Same—Necessity for Bona Fide Attempt to Organize.

It is also essential to de facto corporate existence that there shall have been a bona fide attempt to organize under the law, and at least a colorable compliance with the law in such attempt. "To give to a body of men assuming to act as a corporation, where there has been no attempt to comply with the provisions of any law authorizing them to become such, the status of a de facto corporation, might open the door to frauds upon the public. It would certainly be impolitic to permit a number of men to have the status of a corporation to any extent merely because there is a law under which they might have become incorporated, and they have agreed among themselves to act, and they have acted, as a corporation. * * * 'Color of apparent organization under some charter or enabling act'²⁴ does not mean that there shall have been a full compliance with what the law requires to be done, nor a substantial compliance. A substantial compliance will make a corporation de jure. But there must be an apparent attempt to perfect an organization under the law. There being such apparent attempt to perfect an organization, the failure as to some substantial requirement will prevent the corporation from being a corporation de jure; but, if there be user pursuant to such attempted organization, it will not prevent it being a corporation de facto."²⁵

²² Norton v. Shelby Co., 118 U. S. 442, 6 Sup. Ct. 1121.

²³ Ante, p. 89.

²⁴ The court had previously quoted from Taylor on Corporations: "When a body of men are acting as a corporation under color of apparent organization, in pursuance of some charter or enabling act, their authority to act as a corporation cannot be questioned collaterally." Tayl. Corp. 145.

²⁵ Finnegan v. Noerenberg, 52 Minn. 239, 53 N. W. 1150. And see Bash v. Mining Co., 7 Wash. 122, 34 Pac. 464; Eaton v. Walker, 76 Mich. 579, 43 N. W. 638.

Same—Sufficiency of Compliance with Law.

There are some cases that hold, and some that seem to hold, that there cannot be even a *de facto* corporation unless the incorporators have substantially complied with all the conditions precedent prescribed by the statute; that, without such compliance, the pretended corporation does not come into existence for any purpose; and that, in the absence of elements of estoppel, the objection may be raised by a private individual as well as by the state, and collaterally as well as directly.²⁶ These cases, however, are contrary to the great weight of authority, and some of them are not easily reconciled with other decisions of the same court. To constitute a corporation *de facto* there must, it is true, be a colorable compliance with the statute, but there need not be more. There need not be a substantial compliance. A substantial compliance makes the body a corporation *de jure*.²⁷ As was said by the Minnesota court, if there be an "apparent attempt to perfect an organization, the failure as to some substantial requirement will prevent the corporation from being a corporation *de jure*; but, if there be user pursuant to such attempted organization, it will not prevent it being a corporation *de facto*."²⁸ That a colorable or apparent compliance, in good faith, with the provisions of the law, is sufficient, is shown by cases in almost all of the states.²⁹ Some of the cases in

²⁶ Thus, in *Utley v. Tool Co.*, 11 Gray (Mass.) 139, a case in which it was sought to charge the defendants as stockholders of an alleged corporation with personal liability for its debts, the defense was that there were no written articles of agreement in the organization of the alleged corporation, as required by the statute under which the organization was attempted, and the defense was allowed. So, in *Bigelow v. Gregory*, 73 Ill. 197, certain persons undertook to organize a corporation under a general law which required the articles of association to be published in a certain way, and a certificate of the purposes of the incorporation to be filed in certain public offices; but they failed to comply with these provisions. It was held that there was no corporation *de facto*, though articles of association were executed, a common name adopted, and business conducted under it; and the associates were held liable as partners for goods sold to them. See, also, *Montgomery v. Forbes*, 148 Mass. 249, 19 N. E. 342; *1 Cumming, Cas. Priv. Corp.* 69; *Kaiser v. Bank*, 56 Iowa, 104, 8 N. W. 772; *Shep. Cas. Corp.* 268; *Hurt v. Salisbury*, 55 Mo. 310; *McLennan v. Hopkins*, 2 Kan. App. 260, 41 Pac. 1061.

²⁷ Ante, p. 59.

²⁸ *Finnegan v. Noerenberg*, 52 Minn. 239, 53 N. W. 1150.

²⁹ See *Thompson v. Candor*, 60 Ill. 244; *Bushnell v. Machine Co.*, 138 Ill. 67.

which the courts have allowed a collateral attack on the authority of an association to exercise corporate powers, where there was a valid law under which it might be incorporated, a bona fide attempt at incorporation under it, and user of corporate powers, may perhaps be explained on the ground that the court did not consider that there had been even a colorable or apparent compliance with the law.³⁰

Same—Necessity for User of Corporate Powers.

To constitute a de facto corporation it is also essential that the parties shall have assumed in some way the appearance of a corporation, and shall have pretended to act as a corporate body. If, after an attempt at incorporation, in which conditions precedent are not complied with, the directors named in the articles never meet, and no stock is issued nor corporate act done, the association is not a corporation de facto.³¹ The mere fact that the owners of a mine use a corporate name does not make a corporation de facto, where no corporate act is performed, and no steps have been taken to incorporate.³² As was said in a Michigan case, however, "if the law exists, and the record exhibits a bona fide attempt to organize under it, very slight evidence of user beyond this is all that can be required."³³

27 N. E. 596; *Miami Powder Co. v. Hotchkiss*, 17 Ill. App. 622; *Hudson v. Seminary Corp.*, 113 Ill. 618; *Duggan v. Investment Co.*, 11 Colo. 113, 17 Pac. 105. In *Duggan v. Investment Co.*, supra, it was sought to avoid a mortgage given by a corporation on the ground that its certificate of incorporation was defective because it was not acknowledged as required by the statute. The court said: "We are aware of the distinction between mere omissions or irregularities, and what are called 'prerequisites' of the statutes. The distinction may well be taken in a direct proceeding or other exceptional cases where strict proof is required, but we do not regard it as having any controlling place in the case at bar. What is or what is not a prerequisite is often a difficult question for a professional man, and much more for a layman, to determine. To cast such a burden upon the public as between its individual members is to lose sight of the reason for, and largely abrogate, the salutary rule respecting de facto corporations."

³⁰ Compare *Finnegan v. Noerenberg*, 52 Minn. 239, 53 N. W. 1150, with *Johnson v. Corser*, 34 Minn. 355, 25 N. W. 799.

³¹ *Martin v. Deetz*, 102 Cal. 55, 36 Pac. 368.

³² *Bash v. Mining Co.*, 7 Wash. 122, 34 Pac. 462.

³³ *Eaton v. Walker*, 76 Mich. 579, 43 N. W. 638.

Same—Where Attempted Organization is a Fraud upon the Act.

If the attempted organization of a corporation was a fraud upon the act under which corporate existence is claimed, the better opinion is that there is no corporation, even de facto. Thus, where citizens of New Jersey went over into New York, and there attempted to form a corporation under the laws of that state for the purpose of doing business in New Jersey, it was held that there was no corporation de facto, since, under the circumstances of that particular case, the attempted organization was a fraud upon the laws of New York.⁸⁴ So, where persons not named in a charter creating a corporation to be located at a certain place, got control of the charter, and attempted to establish a corporation under it, to be located at a different place, it was held that the pretended corporation was not even a de facto corporation.⁸⁵

The Doctrine of De Facto Corporations Distinct from the Doctrine of Estoppel.

Much of the confusion in the cases as to corporations de facto results from a failure to distinguish between the doctrine of corporations de facto and the doctrine of equitable estoppel.⁸⁶ They are not the same thing, but entirely different doctrines. No elements of estoppel are necessary to prevent a private individual from objecting to the existence of a corporation de facto; and, as we shall see, a man may, on equitable grounds, be estopped to question the corporate character of an association that is not even a corporation de facto. The rule relating to de facto corporations, said the Minnesota court, "is not founded upon any principle of estoppel, as is sometimes assumed, but upon the broader principles of common justice and public policy. It would be unjust and intolerable if, under such circumstances, every interloper and intruder were allowed thus to take advantage of every informality or irregularity of or-

⁸⁴ Hill v. Beach, 12 N. J. Eq. 31. See Empire Mills v. Alston Grocery Co. (Tex. App.) 15 S. W. 200, 505, Shep. Cas. Corp. 64.

⁸⁵ Booth v. Wonderly, 36 N. J. Law, 250. Cf. Elizabethtown Gas Light Co. v. Green, 46 N. J. Eq. 118, 18 Atl. 844; Id., 49 N. J. Eq. 329, 24 Atl. 560.

⁸⁶ For examples, see Hamilton v. Railroad Co., 144 Pa. St. 34, 23 Atl. 53; Bates v. Wilson, 14 Colo. 140, 24 Pac. 99, 104; Foster v. Moulton, 35 Minn. 458, 29 N. W. 155.

ganization.”⁸⁷ The law forbids a private individual to question the right of a corporation de facto to existence as a corporation, not because of any conduct on his part which renders it inequitable to allow him to do so, for the doctrine extends to persons who have had no dealings whatever with the corporation, but because, irrespective of any question as to his position or conduct, it is contrary to public policy to allow any private individual to do so. No man can deny that a particular association is a corporation de facto, if he has so acted as to be equitably estopped, but, if not so estopped, he can. No man at all can question the corporate existence of a de facto corporation. This distinction is recognized by the Alabama court in a case in which it is said that, before a suit can be maintained by an alleged corporation, its actual or de facto existence must be proved, “or else a state of facts shown which will operate to estop the defendant from denying such de facto existence.”⁸⁸ In a great many cases it is said that “a person who has entered into a contract” with a “de facto” corporation in its corporate name and capacity cannot, in the absence of fraud, afterwards disregard the existence of the corporation, and sue the stockholders individually as partners on the contract, or defeat an action by the corporation on the contract.⁸⁹ This is a confusion of principles. They would be estopped in such a case to deny the existence of the corporation, whether it is a corporation de facto or not. These cases, therefore, are more properly considered under the doctrine of estoppel. If the corporation is a de facto one, then it is not necessary that a private individual shall have dealt with it in order that he may be prevented from questioning its corporate existence.

In an Ohio case, the plaintiff admitted that persons who have recognized the existence of a pretended corporation by their transactions with it as a corporation are estopped to deny its corporate

⁸⁷ *East Norway Lake Church v. Froislie*, 37 Minn. 447, 35 N. W. 260. And see *Society Perun v. Cleveland*, 43 Ohio St. 481, 3 N. E. 357 (collecting cases); *Williamson v. Association*, 89 Ind. 389; *Pape v. Bank*, 20 Kan. 440.

⁸⁸ *Schloss v. Trade Co.*, 87 Ala. 411, 6 South. 380.

⁸⁹ See *Snider's Sons Co. v. Troy*, 91 Ala. 224, 8 South. 658; *Swartwout v. Railroad Co.*, 24 Mich. 390; *Butchers' & Drovers' Bank v. McDonald*, 130 Mass. 264, 1 Cumming. Cas. Priv. Corp. 420.

existence; but it was contended that, as the plaintiff had engaged in no transactions with the alleged corporation in this case, he was free to challenge its existence as a corporation *de facto* as well as *de jure*,—the argument being that “no case can be found where it is held that there is a corporation *de facto* against persons who have in no way recognized its existence as a corporation;” and that “the notion of a *de facto* corporation is based on the doctrine of estoppel. When estoppel cannot be invoked, there can be no *de facto* corporation.” The court, however, declined to take this view, and held that it is a rule, entirely irrespective of any question of estoppel, that no private individual can attack the corporate character of a *de facto* corporation. In its opinion the court said: “The theory that a *de facto* corporation has no real existence—that it is a mere phantom, to be invoked only by that rule of estoppel which forbids a party who has dealt with a pretended corporation to deny its corporate existence—has no foundation, either in reason or authority. A *de facto* corporation is a reality. It has an actual and substantial legal existence. It is, as the term implies, a corporation. * * * It is bound by all such acts as it might rightfully perform as a corporation *de jure*. Where it has attempted, in good faith, to assume corporate powers; where its proceedings in that behalf are colorable, and are approved by those officers of the state who are authorized to act in that regard; where it has honestly proceeded for a number of years, without interference from the state, to transact business as a corporation; has been reputed and dealt with as a duly-incorporated body, and valuable rights and interests have been acquired and transferred by it,—no substantial reason is suggested why its corporate existence, in a suit involving such transactions, should be subject to attack by any other party than the state, and then only when it is called upon, in a direct proceeding for that purpose, to show by what authority it assumes to be a corporation.” ⁴⁰

⁴⁰ *Society Perun v. Cleveland*, 43 Ohio St. 481, 8 N. E. 357.

ESTOPPEL TO DENY CORPORATE EXISTENCE.

43. Where persons pretend to form a corporation, and assume to exercise corporate powers, an estoppel to deny that they are a corporation operates as against

- (a) The persons who so hold themselves out as a corporation.**
- (b) The pretended corporation itself.**
- (c) Third persons who deal with the association as a corporation, except in the cases hereafter mentioned.**

44. EXCEPTIONS—To the rule above stated there are exceptions. Though there are some conflicting decisions, by the weight of authority the doctrine does not apply

- (a) Where the dealings relied upon as an estoppel are not such as to show recognition of the association as a corporation.**
- (b) Where there are no equitable grounds for applying it, and, a fortiori, where to apply it would be inequitable.**
- (c) A few cases hold that the doctrine does not apply where the assumption of corporate powers was unlawful as being in violation of a prohibitory law.**
- (d) In a few states the doctrine is held to apply to such associations only as are at least corporations de facto; but by the weight of authority it is not to be so limited.**

It is a well-settled rule, subject to very few, if any, exceptions, that, where persons undertake to form a corporation, and afterwards assume to act as a corporate body, neither they nor the association can dispute its corporate existence and authority to act as such, when it is sued as a corporation on a contract into which it has entered in that character.⁴¹ Nor under such circumstances

⁴¹ Scheufler v. Grand Lodge, 45 Minn. 256, 47 N. W. 799; Perine v. Grand Lodge, 48 Minn. 82, 50 N. W. 1022; Narragansett Bank v. Atlantic Silk Co., 3 Metc.

can the associates deny the corporate character of the association, in order to escape statutory liability for its debts.⁴² Nor can they do so in order to avoid liability on their subscriptions to stock in the pretended corporation, when sued thereon either by it, or by its creditors, or by a receiver or assignee.⁴³ The estoppel also oper-

(Mass.) 287; *Farmers' Loan & Trust Co. v. Toledo, A. A. & N. M. Ry. Co.*, 67 Fed. 49; *Callender v. Railroad Co.*, 11 Ohio St. 516; *Stewart Paper Manuf'g Co. v. Rau*, 92 Ga. 511, 17 S. E. 748; *Fitzpatrick v. Rutter*, 160 Ill. 282, 43 N. E. 392; *Hamilton v. Railroad Co.* (Pa. Sup.) 23 Atl. 53; *Bon Aqua Imp. Co. v. Standard Fire Ins. Co.*, 34 W. Va. 764, 12 S. E. 771; *Independent Order of Mutual Aid v. Paine*, 122 Ill. 625, 14 N. E. 42. See, also, *Dooley v. Cheshire Glass Co.*, 15 Gray (Mass.) 494, 1 Cumming, Cas. Priv. Corp. 418.

⁴² *Slocum v. Gas-Pipe Co.*, 10 R. I. 112; *Slocum v. Warren*, Id. 116; *Building & Loan Ass'n of Dakota v. Chamberlain*, 4 S. D. 271, 56 N. W. 897; *Corey v. Morrill*, 61 Vt. 598, 17 Atl. 841; *Hamilton v. Railroad Co.*, 144 Pa. St. 34, 23 Atl. 53; *Freeland v. Insurance Co.*, 94 Pa. St. 504; *Wheelock v. Kost*, 77 Ill. 296; *McCarthy v. Lavasche*, 89 Ill. 270; *McDonnell v. Insurance Co.*, 85 Ala. 401, 5 South. 120; *Eaton v. Aspinwall*, 19 N. Y. 119; *McClinch v. Sturgis*, 72 Me. 288; *Aultman v. Waddle*, 40 Kan. 195, 19 Pac. 730.

⁴³ *Wadesboro Cotton Mills Co. v. Burns*, 114 N. C. 353, 19 S. E. 238; *Hickling v. Wilson*, 104 Ill. 54; *Weinman v. Railway Co.*, 118 Pa. St. 192, 12 Atl. 288; *Parker v. Railroad Co.*, 33 Mich. 23; *Cravens v. Mills Co.*, 120 Ind. 6, 21 N. E. 981; *Anderson v. Railroad Co.*, 12 Ind. 376; *Chubb v. Upton*, 95 U. S. 665; *American Homestead Co. v. Linigan*, 46 La. Ann. 1118, 15 South. 369; *Upton v. Hansbrough*, 3 Biss. 417, Fed. Cas. No. 16,801; *Dutchess Cotton Manufactory v. Davis*, 14 Johns. (N. Y.) 238; *Black River & U. R. Co. v. Clarke*, 25 N. Y. 208; *Chester Glass Co. v. Dewey*, 16 Mass. 94; *Home Stock Ins. Co. v. Sherwood*, 72 Mo. 461; *Ohio & M. R. Co. v. McPherson*, 35 Mo. 13; *South Bay Meadow Dam Co. v. Gray*, 30 Me. 547; *Montpelier & W. R. R. Co. v. Langdon*, 46 Vt. 284. This rule has no application to one who subscribes for stock previous to and in anticipation of incorporation, and who has not by his subsequent acts acquiesced in the mode of incorporation. In such a case it is an implied condition of his subscription that the proposed corporation shall be legally and regularly organized; and, if it is not, he may set it up as a defense when sued on his subscription. *Schloss v. Trade Co.*, 87 Ala. 411, 6 South. 360; *Columbia Electric Co. v. Dixon*, 46 Minn. 463, 49 N. W. 244; post, p. 103, note 50. If, however, a subscriber to stock in a corporation to be formed takes active part in its organization, or in its management after organization, he cannot be heard to say that it was not legally organized. *Danbury & N. R. Co. v. Wilson*, 22 Conn. 435, 456; *Phoenix Warehousing Co. v. Badger*, 67 N. Y. 204; *Schenectady & S. Plank Road Co. v. Thatcher*, 11 N. Y. 102; *Ohio & M. R. Co. v. McPherson*, 35 Mo. 13; *Oanfield v. Gregory*, 66 Conn. 9, 33 Atl. 536.

ates in actions and controversies between the associates themselves.⁴⁴ Not only may the associates themselves, and the association or pretended corporation, be thus estopped, but third persons may be estopped by dealing with the association as a corporation. Thus, it has frequently been held that entering into a contract with an association as a corporation will operate as an estoppel to dispute its existence as a corporation, in an action brought on the contract, unless there are special circumstances to take the case out of the general rule, whether it be brought by the pretended corporation,⁴⁵ or by the other party, in disregard of the corporate existence of the association, to charge the members in-

⁴⁴ See *Bushnell v. Machine Co.*, 188 Ill. 67, 27 N. E. 596.

⁴⁵ *Methodist Church v. Pickett*, 19 N. Y. 482, 1 Cumming, Cas. Priv. Corp. 407; *Commercial Bank v. Pfeiffer*, 108 N. Y. 242, 15 N. E. 311; *Stoutimore v. Clark*, 70 Mo. 471; *Minnesota Gaslight Economizer Co. v. Denslow*, 46 Minn. 171, 48 N. W. 771; *Jones v. Foundry Co.*, 14 Ind. 89; *Fresno Canal & Irr. Co. v. Warner*, 72 Cal. 379, 14 Pac. 37; *Chubb v. Upton*, 95 U. S. 665; *Swartwout v. Railroad Co.*, 24 Mich. 390; *Stofflet v. Strome*, 101 Mich. 197, 59 N. W. 411; *Booske v. Ice Co.*, 24 Fla. 550, 5 South. 247; *School Dist. No. 61 v. Alderson*, 6 Dak. 145, 41 N. W. 466; *Cahall v. Association*, 61 Ala. 232; *Douglass County Com'rs v. Bolles*, 94 U. S. 104; *Tarbell v. Page*, 24 Ill. 46; *Winget v. Association*, 128 Ill. 67, 21 N. E. 12; *Columbia Electric Co. v. Dixon*, 46 Minn. 463, 49 N. W. 244; *Building & Loan Ass'n v. Chamberlain*, 4 S. D. 271, 56 N. W. 897; *Butchers' & D. Bank v. McDonald*, 180 Mass. 264, 1 Cumming, Cas. Priv. Corp. 420; *Worcester Medical Inst. v. Harding*, 11 Cush. (Mass.) 285; *Lehman v. Warner*, 61 Ala. 455; *Close v. Glenwood Cemetery*, 107 U. S. 477, 2 Sup. Ct. 267; *Oregonian Ry. Co. v. Oregon Ry. & Nav. Co.*, 23 Fed. 232; *Grangers' Business Ass'n v. Clark*, 67 Cal. 634, 8 Pac. 445; *South Bay Meadow Dam Co. v. Gray*, 30 Me. 547; *Hassinger v. Ammon*, 160 Pa. St. 245, 28 Atl. 679; *Bank of Shasta v. Boyd*, 99 Cal. 604, 34 Pac. 337. Thus, the grantor in a deed in favor of a body professing to be a corporation and acting as such, and any person claiming under him, is estopped to deny the corporate existence of the grantee, for the purpose of defeating the deed. *Broadwell v. Merritt* (Mo. Sup.) 1 S. W. 855; *Whitney v. Robinson*, 53 Wis. 309, 10 N. W. 512. And the execution of a note or bond payable to a body as a corporation is an admission by the maker or obligor of its corporate existence, which will estop him from denying it. *Stoutimore v. Clark*, 70 Mo. 471; *Vater v. Lewis*, 38 Ind. 288; *Brickley v. Edwards*, 131 Ind. 8, 30 N. E. 708; *John v. Bank*, 2 Blackf. (Ind.) 367, 20 Am. Dec. 119; *School Dist. No. 61 v. Alderson*, 6 Dak. 145, 41 N. W. 466; *Booske v. Ice Co.*, 24 Fla. 550, 5 South. 247.

dividually as partners.⁴⁶ As to the latter proposition, however, there is some doubt, and there are well-considered cases against it.⁴⁷

Necessity for Recognition of Corporate Existence.

To warrant holding a person estopped from denying the existence of a corporation because he has dealt with it, his dealings must have been such as to show a recognition of the corporate character of the body. A man cannot be so estopped by acts which are just as consistent with the existence of an unincorporated association as of one incorporated, for "estoppels never arise from ambiguous facts; they must be established by those that are unequivocal, and not susceptible of two constructions."⁴⁸ Thus, the mere fact that a man accepted the office of treasurer of an association will not estop him from denying that the association was a corporation; nor will the members of a religious association, for instance, be estopped to deny its existence as a corporation by the fact that they held the ordinary meetings of a religious society, passed by-laws, elected officers, etc., for these acts are just as consistent with the existence of an unincorporated association as of a corporation.⁴⁹ On the same principle it has been held that, though a person who has co-operated in the organization and acts of a body as a corporation will be estopped from disputing its corporate character, a person who merely subscribes for stock in a corporation not yet formed, and makes a payment thereon preliminary to its organization, but who does nothing to recognize the body as duly incorporated, will

⁴⁶ See *Snider's Sons' Co. v. Troy*, 91 Ala. 224, 8 South. 658; *Cochran v. Arnold*, 58 Pa. St. 399. And see *Shields v. Land Co.*, 94 Tenn. 123, 28 S. W. 668; *Phinizy v. Railroad Co.*, 62 Fed. 678; *Bradford v. Railroad Co.*, 142 Ind. 383, 40 N. E. 741; *Black River Imp. Co. v. Holway*, 85 Wis. 344, 55 N. W. 418; *Johnston v. Gumbel* (Miss.) 19 South. 100. In the latter case it was held that creditors of a corporation, having dealt with it in its corporate capacity, cannot attack an assignment by it on the ground of irregularities in its organization.

⁴⁷ Post, p. 109, notes 71-73.

⁴⁸ *Fredenburg v. Lyon Lake M. E. Church*, 37 Mich. 476. See *Schloss v. Trade Co.*, 87 Ala. 411, 6 South. 360; *De Witt v. Hastings*, 69 N. Y. 518; *Clark v. Jones*, 87 Ala. 474, 6 South. 362.

⁴⁹ *Fredenburg v. Lyon Lake M. E. Church*, supra; *Kirkpatrick v. United Presbyterian Church of Keota*, 63 Iowa, 372, 19 N. W. 272; *Trustees, etc., of M. E. Church of Newark v. Clark*, 41 Mich. 730, 3 N. W. 207.

not be estopped to deny its de facto existence.⁵⁰ And a person who contracts with an association in ignorance of its claim to corporate existence is not thereby estopped to sue the associates as partners.⁵¹ The mere fact that in a contract with an association it is designated by a name which is appropriate to a corporate body does not show a recognition or admission of its existence as a corporation. It merely shows an admission of the existence of an association acting under that name.⁵²

Doctrine of Estoppel is Based on Equitable Grounds.

An examination of the cases in which the doctrine of estoppel to deny corporate existence has been applied will show that most of them rest on some basis of conduct, or of benefit obtained, or other cause rendering it inequitable to allow such denial. The doctrine is an equitable one, and should be applied only where there are equitable grounds for applying it. It should never be applied where it would be inequitable to do so.⁵³ Nor should it be applied unless it would be inequitable not to do so. To say, therefore, without qualification, that a person who deals with an association as a corporation is estopped to deny its existence as a corporation, is too broad. It is perfectly right that a person who deals with an association as

⁵⁰ Schloss v. Trade Co., supra. And see Columbia Electric Co. v. Dixon, 46 Minn. 463, 49 N. W. 244; Capps v. Prospecting Co., 40 Neb. 470, 58 N. W. 958; Indianapolis F. & M. Co. v. Herkimer, 46 Ind. 142; Rikoff v. Machine Co., 68 Ind. 388; Dorris v. Sweeney, 60 N. Y. 463; Richmond Factory Ass'n v. Clarke, 61 Me. 351.

⁵¹ In Guckert v. Hacke, 159 Pa. St. 303, 28 Atl. 249, it was held that where a person contracts with an association of persons, and becomes their creditor, without any knowledge that they claim to be a corporation instead of partners, and there is nothing to put him on inquiry, he is not estopped to sue the members as partners, and show that they have failed to comply with the law under which they claim corporate existence; and, further, that he cannot be estopped by taking their corporate note for the debt after knowledge of their claim to corporate existence, for the relation of the parties has been fixed by their status when the original contract was made. And see Eaton v. Walker, 76 Mich. 579, 43 N. W. 638; Duke v. Taylor (Fla.) 19 South. 172. Cf. Fitzpatrick v. Rutter, 160 Ill. 282, 43 N. E. 392.

⁵² Holloway v. Railroad Co., 23 Tex. 465; Welland Canal Co. v. Hathaway, 8 Wend. (N. Y.) 480. See Jones v. Foundry Co., 14 Ind. 89.

⁵³ Doyle v. Mizner, 42 Mich. 332, 3 N. W. 968. And see Elstey Manuf'g Co. v. Runnels, 55 Mich. 130, 20 N. W. 823.

a corporation, knowing that it is not, should be left in the position that he has thus assumed, and be precluded from denying that the body is a corporation in actions growing out of the transaction.⁵⁴ When, however, a person deals with a body as a corporation, which the members hold out as a corporation, and which he believes to be a corporation, there should be something more than the mere fact of his dealings to estop him.⁵⁵ If, in such a case, he derives a benefit from the association, and assumes an obligation to pay therefor, as where a person borrows money or purchases goods from a pretended corporation, it is equitable that he should be estopped to deny its corporate existence in order to escape liability on his obligation.⁵⁶ On the other hand, however, if a person deals with a pretended corporation, believing it to be a corporation, and, instead of receiving a benefit himself, confers a benefit upon the associates, he ought not, from the mere fact that he dealt with them as a corporation, to be estopped to deny their corporate existence, and hold them individually liable. Though there are cases to the contrary,⁵⁷ there are many cases which hold that there is no estoppel under such circumstances.⁵⁸

Unlawful Assumption of Corporate Powers.

It has been said that the doctrine of estoppel does not apply, so as to prevent one who recognizes a pretended corporation by con-

⁵⁴ See *Whitney v. Wyman*, 101 U. S. 392.

⁵⁵ *Williams v. Hewitt*, 47 La. Ann. 1076, 17 South. 496.

⁵⁶ Ante, p. 101, and cases cited.

⁵⁷ See *Snider's Sons' Co. v. Troy*, 91 Ala. 224, 8 South. 658; *Cochran v. Arnold*, 58 Pa. St. 399.

⁵⁸ In *Williams v. Hewitt*, 47 La. Ann. 1076, 17 South. 496, the defendants conducted a banking business as a corporation, when they were not a corporation because of noncompliance with the statute under which they pretended to organize. The plaintiff deposited money with them, believing that they were a corporation. Afterwards he brought suit against them individually as partners, to recover the amount of the deposit, and it was held that he was not estopped. And there are many cases in which a person who has sold goods to a pretended corporation has been permitted, on discovery that there was no corporation, to sue the associates as partners. *Montgomery v. Forbes*, 148 Mass. 249, 19 N. E. 342, 1 Cumming, Cas. Priv. Corp. 69. And see *Bigelow v. Gregory*, 73 Ill. 197; *Abbott v. Refining Co.*, 4 Neb. 416. Contra, *Snider's Sons' Co. v. Troy*, 91 Ala. 224, 8 South. 658; *Cochran v. Arnold*, 58 Pa. St. 399.

tracting with it from afterwards denying its corporate character, where the assumption of corporate powers by the body was unlawful, as being in violation of a prohibitory law, or as being for an illegal purpose. Any dealings with such a body would be illegal and void, and could not give rise to a cause of action.⁵⁹

Doctrine of Estoppel not Limited to De Facto Corporations.

This question has already been somewhat referred to.⁶⁰ In *Swartwout v. Michigan Air-Line R. Co.*,⁶¹ Judge Cooley said: "Where there is a corporation de facto, with no want of legislative power to its due and legal existence, when it is proceeding in the performance of corporate functions, and the persons are dealing with it on the supposition that it is what it professes to be, and the questions are only whether there has been exact regularity, and strict compliance with the provisions of the law relating to corporations, it is plainly a dictate alike of justice and public policy that, in controversies between the de facto corporation and those who have entered into contract relations with it, as corporators or otherwise, such questions should not be suffered to be raised." This dictum has been often quoted, and the doctrine of estoppel has been similarly stated by many other courts.⁶² The dictum in these cases is broad enough to imply that the doctrine of estoppel applies to de facto corporations only; but in this respect it is mere dictum, and nothing more. They do not so hold, and from other decisions of some of the same courts it seems evident that it was not intended

⁵⁹ See 1 *Thomp. Corp.* § 533; *Wright v. Lee*, 2 S. D. 596, 51 N. W. 706; *Building & Loan Ass'n of Dakota v. Chamberlain* (S. D.) 56 N. W. 897; *Oregonian Ry. Co. v. Oregon Ry. & Nav. Co.*, 28 Fed. 233; *Empire Mills v. Alston Grocery Co.* (Tex. App.) 15 S. W. 200, 505; *Shep. Cas. Corp.* 64. But see *Lincoln Building & Sav. Ass'n v. Graham*, 7 Neb. 173.

⁶⁰ Ante, p. 96.

⁶¹ 24 Mich. 390.

⁶² See the dictum in *Snider's Sons' Co. v. Troy*, 91 Ala. 224, 8 South. 658; *Butchers' & Drovers' Bank of St. Louis v. McDonald*, 130 Mass. 264, 1 Cumming, Cas. Priv. Corp. 420; *Bushnell v. Machine Co.*, 138 Ill. 67, 27 N. E. 596; *Merchants' & Manufacturers Bank v. Stone*, 38 Mich. 779; *Merriman v. Magiveny*, 12 Heisk. (Tenn.) 494; *Eaton v. Aspinwall*, 19 N. Y. 119; *Cochran v. Arnold*, 58 Pa. St. 399; *Central Agricultural & Mechanical Ass'n v. Alabama Gold Life Ins. Co.*, 70 Ala. 120.

to so hold.⁶³ There are some decisions, however, which do expressly hold that the doctrine only applies to associations that are at least corporations de facto; that it does not apply, for instance, to an association that has never had any corporate existence at all, either in law or in fact, as where persons have attempted to organize a corporation, and have assumed to act as such, without any legislative authority at all, or under an unconstitutional law.⁶⁴ These decisions do not seem right. They confuse the doctrine relating to de facto corporations and the doctrine of estoppel, which, as we have seen, are not the same, and which are founded on different reasons. "The rule relating to corporations de facto is not founded upon any principle of estoppel, as is sometimes assumed, but upon the broader principles of common justice and public policy. It would be unjust and intolerable if, under such circumstances, every interloper and intruder were allowed thus to take advantage

⁶³ Compare, with the above, *Cahall v. Association*, 61 Ala. 232; *Schloss v. Trade Co.*, 87 Ala. 411, 8 South. 360; *Estey Manuf'g Co. v. Runnels*, 55 Mich. 130, 20 N. W. 823; *Stofflet v. Strome*, 101 Mich. 197, 59 N. W. 411. In *Schloss v. Trade Co.*, supra, it was said that, before a suit can be maintained by an alleged corporation, its actual or de facto existence must be proved, "or else" a state of facts shown which will estop the defendant from denying "such de facto existence." And further on it is again said that a subscriber to stock, like any other person, may be estopped from disputing "the de facto existence" of a corporation. This clearly implies that the doctrine of estoppel applies to associations which pretend to be a corporation, but which have not even a de facto existence as such. In *Estey Manuf'g Co. v. Runnels*, supra, it was said: "Where a body assumes to be a corporation, and acts under a particular name, a third party dealing with it under such assumed name is estopped to deny its corporate existence. Such is the general rule founded upon equitable principles, and, if any exceptions exist, it is only where there are no facts which make it legally unjust to forbid its denial." The rule here is not limited to de facto corporations.

⁶⁴ *Heaston v. Railroad Co.*, 16 Ind. 275, 279, 1 Cumming, Cas. Priv. Corp. 417, W. D. Smith, Cas. Corp. 20, Shep. Cas. Corp. 134; *Snyder v. Studebaker*, 19 Ind. 462; *Harriman v. Southam*, 16 Ind. 190; *Jones v. Hardware Co.*, 21 Colo. 263, 40 Pac. 457; *Brandenstein v. Hoke*, 101 Cal. 131, 35 Pac. 562. And see *Empire Mills v. Alston Grocery Co.* (Tex. App.) 15 S. W. 505; *Boyce v. Trustees*, 46 Md. 359. The dictum in *Eaton v. Walker*, 76 Mich. 579, 43 N. W. 638, seems to support this view; but in this case it was not shown that the plaintiff contracted with the defendants as a corporation, or that he even knew that they pretended to be a corporation.

of every informality or irregularity of organization.”⁶⁵ In reason, the reverse of this proposition ought to be equally true, namely, that the rule by which a person is estopped from denying the corporate character of an association which he has recognized as a corporation by dealing with it as such does not depend upon the existence of the body as a *de facto* corporation. There are many cases in which the rule is stated without limiting it to *de facto* corporations, and there are cases which expressly hold that it is not so limited; that it applies, for instance, where the law under which corporate existence is claimed is unconstitutional.⁶⁶ It was said by the supreme court of the United States: “Where a shareholder of a corporation is called upon to respond to a liability as such, and where a party has contracted with a corporation and is sued upon the contract, neither is permitted to deny the existence or the legal validity of such corporation. To hold otherwise would be contrary to the plainest principles of reason and of good faith, and involve a mockery of justice. Parties must take the consequences of the position they assume. They are estopped to deny the reality of

⁶⁵ *East Norway Lake Church v. Froislie*, 37 Minn. 447, 35 N. W. 260. And see *Society Perun v. Cleveland*, 43 Ohio St. 481, 3 N. E. 357 (collecting cases).

⁶⁶ *Minnesota Gaslight Economizer Co. v. Denslow*, 46 Minn. 171, 48 N. W. 771; *Snyder v. Bank, Breese* (Ill.) 161; *McCarthy v. Lavasche*, 89 Ill. 270; *Dows v. Naper*, 91 Ill. 44; *Winget v. Association*, 128 Ill. 67, 21 N. E. 12; *Building & Loan Ass'n v. Chamberlain*, 4 S. D. 271, 56 N. W. 897 (collecting cases); *Corey v. Morrill*, 61 Vt. 598, 17 Atl. 841; *Freeland v. Insurance Co.*, 94 Pa. St. 504; *Weinman v. Railway Co.*, 118 Pa. St. 192, 12 Atl. 288; *Board of Com'rs of City of St. Louis v. Shields*, 62 Mo. 247; *Broadwell v. Merritt* (Mo.) 1 S. W. 855; *Fresno Canal & Irr. Co. v. Warner*, 72 Cal. 379, 14 Pac. 37; *American Homestead Co. v. Linigan*, 46 La. Ann. 1118, 15 South. 369; *Bates v. Wilson*, 14 Colo. 140, 24 Pac. 99; *Bashford-Burmister Co. v. Agua Fria Copper Co.* (Ariz.) 35 Pac. 983; *Pape v. Bank*, 20 Kan. 440. “It is too well settled now to be controverted that a party who contracts with a corporation, whether it be by subscription to its stock, or by promissory note, bond, mortgage, or other form of contract, is estopped from denying the existence of the corporation.” *Lehman, Durr & Co. v. Warner*, 61 Ala. 455, 466. “One who deals with a corporation as existing in fact is estopped to deny, as against the corporation, that it has been legally organized.” *Close v. Cemetery*, 107 U. S. 477, 2 Sup. Ct. 267. “It is hardly possible that one will be suffered to obtain the goods of another, doing business as a corporation, and retaining the goods, defeat a recovery by alleging the illegality of the act under which the corporation was formed. We do not care to countenance such a result.” *Bashford-Burmister Co. v. Agua Fria Copper Co.*, *supra*

the state of things which they have made appear to exist, and upon which others have been led to rely. Sound ethics require that the apparent, in its effects and consequences, should be as if it were real, and the law properly so regards it."⁶⁷ If the doctrine were limited to de facto corporations, it would be unnecessary. Grounds of estoppel are not necessary to prevent a private individual, whoever he may be, from attacking the existence of a de facto corporation.⁶⁸

LIABILITY OF ASSOCIATES AS PARTNERS.

45. Where persons hold themselves out as a corporation, and contract as such, without having even a de facto corporate existence, most courts hold that persons dealing with them, if not estopped to deny their corporate existence, may hold them liable as partners. Other courts hold that they are not liable as partners, but that the remedy is against the agents who assume to represent the pretended corporation for breach of implied warranty of authority.

We have just seen that where persons in good faith undertake to organize themselves into a corporation under a valid law authorizing incorporation, and assume corporate powers in pursuance thereof, they constitute a corporation de facto, and, though they may not have complied with the provisions of the law in their organization, they nevertheless have the status of a corporation as against all persons except the state, and that even the state cannot attack their existence as a corporation, except in a direct proceeding for that purpose. In such a case, of course, persons who deal with the body cannot dispute its corporate existence, and hold the associates liable as partners.⁶⁹

We have also seen that, by the weight of authority, even where there is not even a de facto corporation, persons who deal with a

⁶⁷ *Casey v. Galli*, 94 U. S. 673.

⁶⁸ *Ante*, p. 96.

⁶⁹ *Ante*, p. 86; *Stout v. Zulick*, 48 N. J. Law, 599, 7 Atl. 362, *Shep. Cas. Corp.* 275; *Snider's Sons' Co. v. Troy*, 91 Ala. 224, 8 South. 658.

pretended corporation as a corporation will, except under peculiar circumstances, be estopped to deny its existence as a corporation, for the purpose of holding the associates liable as partners.⁷⁰

The question now arises as to the remedy of those who deal with an association which is not even a de facto corporation, and under such circumstances that they are not estopped to deny its corporate existence, as where they deal with the parties in ignorance of their claim of corporate existence. On this question the courts do not agree. In some jurisdictions it is held that persons who contract as a corporation, without a right to do so, cannot be held liable as partners, since they have not contemplated or assented to such a liability. *Fay v. Noble*⁷¹ is a leading case holding this view. In this case the agent of an association which pretended to be a corporation, but which had not been legally organized, borrowed money from the plaintiffs in the name of the association, and gave its note therefor. The plaintiffs sought to recover the money in an action against the associates as partners, but it was held that they could not recover.⁷² There are many other cases to the same effect, though in most of them it will be found that the plaintiff contracted with the association as a corporation, so that he might have been held estopped.⁷³ According to this doctrine, if there is not even a de facto corporation, and the party contracting with the pretended corporation is not estopped to deny its corporate existence, the remedy is against the agent or agents who entered into the contract on

⁷⁰ Ante, p. 99; *Snider's Sons' Co. v. Troy*, 91 Ala. 224, 8 South. 658; *Cochran v. Arnold*, 53 Pa. St. 390.

⁷¹ 7 Cush. (Mass.) 188, 1 Cumming, Cas. Priv. Corp. 420.

⁷² But if a single person assumes, without right, to act and contract as a corporation, his pretended associates being associates in name only, and gives a note in the name of the pretended corporation, he can be sued individually on the note. *Montgomery v. Forbes*, 148 Mass. 249, 19 N. E. 342, 1 Cumming, Cas. Priv. Corp. 69.

⁷³ *Rutherford v. Hill*, 22 Or. 218, 29 Pac. 546; *Trowbridge v. Scudder*, 11 Cush. (Mass.) 83; *First Nat. Bank v. Almy*, 117 Mass. 476; *Ward v. Brigham*, 127 Mass. 24; *Medill v. Collier*, 16 Ohio St. 599; *Humphreys v. Mooney*, 5 Colo. 282; *Planters' & Miners' Bank v. Padgett*, 69 Ga. 159; *Stafford Nat. Bank v. Palmer*, 47 Conn. 443; *Central City Sav. Bank v. Walker*, 66 N. Y. 424; *Jessup v. Carnegie*, 80 N. Y. 441; *Blanchard v. Kaull*, 44 Cal. 440; *Gartside Coal Co. v. Maxwell*, 22 Fed. 197.

behalf of the pretended corporation for breach of implied warranty of authority. "By professing to act for a corporation which does not exist, they put themselves in the position of a person who professes to act as the agent of another person who is really non-existent. Under a well-settled rule, they are therefore personally bound to make good any undertaking which they assume in that character."⁷⁴

In most of the states, perhaps, this rule is not recognized; but it is held that where a pretended corporation is not a corporation de facto, and where persons dealing with it are not, under the rules heretofore explained,⁷⁵ estopped to deny its corporate existence,—as, where they do not know of its claim to corporate existence, or even where they do know of it, if in the particular jurisdiction they are not held to be estopped,—they may hold the associates liable as partners for debts contracted by them in the name of the association.⁷⁶ In some states this rule is, in effect, expressly declared by statute.⁷⁷

⁷⁴ 1 Thomp. Corp. § 418, citing *Medill v. Collier*, 16 Ohio St. 599; *Fay v. Noble*, 7 Cush. (Mass.) 188, 1 Cumming, Cas. Priv. Corp. 420.

⁷⁵ Ante, p. 99.

⁷⁶ *Eaton v. Walker*, 76 Mich. 579, 43 N. W. 638; *Guckert v. Hacke*, 159 Pa. St. 303, 28 Atl. 249; *Empire Mills v. Alston Grocery Co.* (Tex. App.) 15 S. W. 200, 505, Shep. Cas. Corp. 64; *Johnson v. Corser*, 34 Minn. 355, 25 N. W. 799; *Kaiser v. Bank*, 56 Iowa, 104, 8 N. W. 772, Shep. Cas. Corp. 268; *Pettis v. Atkins*, 60 Ill. 454; *Bigelow v. Gregory*, 73 Ill. 197; *Whipple v. Parker*, 29 Mich. 380; *Elliott v. Himrod*, 108 Pa. St. 569; *Garnett v. Richardson*, 35 Ark. 144; *Hill v. Beach*, 12 N. J. Eq. 31; *Abbott v. Refining Co.*, 4 Neb. 416; *Wechselberg v. Bank*, 12 C. C. A. 56, 64 Fed. 90; *Coleman v. Coleman*, 78 Ind. 346; *Martin v. Fewell*, 79 Mo. 401, Shep. Cas. Corp. 271; *Smith v. Warden*, 86 Mo. 382; *Williams v. Hewitt*, 47 La. Ann. 1076, 17 South. 497; *Duke v. Taylor*, 37 Fla. 64, 19 South. 172.

⁷⁷ Post, p. 564. See *Clegg v. Hamilton & Wright County Grange Co.*, 61 Iowa, 121, 15 N. W. 865.

CHAPTER IV.

RELATION BETWEEN CORPORATION AND ITS PROMOTERS.

- 46. Liability of Corporation for Expenses and Services of Promoters.**
- 47. Liability on Contracts by Promoters.**
- 48. Liability of Promoters to Corporation and Stockholders.**

LIABILITY OF CORPORATION FOR EXPENSES AND SERVICES OF PROMOTERS.

- 46. Some courts imply a promise by a corporation to pay for expenses necessarily incurred and services necessarily rendered by promoters, and which inure to the benefit of the corporation; but by the better opinion, in the absence of express provision in the charter or some statute, there is no such liability unless the corporation, after organization, expressly promises to pay.**

Corporations are sometimes made liable by the express provisions of their charter, or by statute, for necessary expenses incurred or services rendered in their promotion. As to the liability in the absence of such provision, there is some difference of opinion. A few courts have held that a corporation is liable at law, upon an implied assumpsit, for expenses legitimately incurred and services legitimately rendered by promoters before its organization, and which were necessary to perfect organization, on the ground that, in accepting the benefit of such expenses and services, it becomes bound to pay therefor, and that no express promise to pay need be shown.¹ The generally accepted doctrine, however, is that the corporation is not liable, unless made so by statute or by its charter, in the absence

¹ *Low v. Railroad Co.*, 45 N. H. 370, 46 N. H. 284; *Hall v. Railroad Co.*, 28 Vt. 401. In these cases a corporation was held liable for services in procuring subscriptions to its capital stock, necessary in order to perfect organization. But in the case last cited charges by promoters for services in procuring an act of incorporation were disallowed, on the ground that the services must be regarded as voluntarily rendered, and there was no promise by the corporation.

of an express promise to pay.* Such a promise is supported by a sufficient consideration, and is binding.

If money is paid by subscribers to promoters preliminary to organization, and the promoters or provisional directors fail to organize according to the prospectus, and abandon the enterprise, after applying the money in payment of expenses in view of organization, the subscribers cannot be made to bear such expenses, and they may recover the money paid by them in an action for money had and received.†

LIABILITY ON CONTRACTS BY PROMOTERS.

47. With regard to the liabilities arising out of contracts entered into by promoters on behalf of a corporation the following rules are established by the weight of authority:

- (a) The promoters are personally liable unless exempt by the terms of the contract.**
- (b) The corporation is not liable unless it has expressly or impliedly adopted the contract after its organization.**
- (c) In Massachusetts it is held that the corporation cannot become a party to the contract even by adoption. But, by the weight of authority, the contract may be adopted by the corporation, and thereby become binding upon it and in its favor.**
- (d) Adoption of the contract is not a ratification, but it is, in effect, the making of a new contract by the corporation, which is to be regarded as made at the date of the adoption.**
- (e) Adoption by the corporation will be implied if it knowingly accepts the benefits of the contract.**

* *Rockford, R. I. & St. L. R. Co. v. Sage*, 65 Ill. 328. *New York & N. H. R. Co. v. Ketchum*, 27 Conn. 170; *Marchand v. Association*, 26 La. Ann. 889; *Melhado v. Railway Co.*, L. R. 9 C. P. 503.

† *Nockels v. Crosby*, 8 Barn. & C. 814; *Walstab v. Spottiswoode*, 15 Mees. & W. 501.

A corporation is not liable on contracts made by its promoters, unless it has adopted them. A promoter, though he may assume to act on behalf of the projected corporation, and not for himself, cannot be treated as an agent of the corporation, for it is not yet in existence; and therefore, when there is nothing more than a contract by a promoter, in which he undertakes to bind the future corporation, it is generally conceded that it cannot be enforced either by or against the corporation.⁴ This is so though the promoters become, at the creation of the corporation, its only stockholders, directors, and officers.⁵ The promoters themselves are personally liable on such contracts, unless the other party agreed to look to some other fund for payment;⁶ and this is the party's only remedy if the corporation, after its organization, has done nothing to bind itself under the principles hereafter explained.

In Massachusetts it is held that, if a contract is made in the name and for the benefit of a projected corporation by its promoters, the corporation cannot become a party to the contract after organization, even by adoption of it.⁷ And it has been so held in some of the English cases.⁸ Most of the courts hold, however, that contracts made by promoters on behalf of a projected corporation, if

⁴ 2 Cook, Stock, Stockh. & Corp. Law, § 707; Weatherford, M. W. & N. W. Ry. Co. v. Granger, 86 Tex. 350, 24 S. W. 795, Shep. Cas. Corp. 33; Battelle v. Pavement Co., 37 Minn. 89, 33 N. W. 327; Franklin Fire Ins. Co. v. Hart, 81 Md. 59; Munson v. Railway Co., 103 N. Y. 58, 8 N. E. 355; Carmody v. Powers, 60 Mich. 26, 26 N. W. 801; Tift v. Bank, 141 Pa. St. 550, 21 Atl. 660; Buffington v. Bardon, 80 Wis. 635, 50 N. W. 776; Penn Match Co. v. Hapgood, 141 Mass. 145, 7 N. E. 22; Abbott v. Hapgood, 150 Mass. 248, 22 N. E. 907; Safety Deposit Life Ins. Co. v. Smith, 65 Ill. 309; Western Screw & Manuf'g Co. v. Cousley, 72 Ill. 531; Gent v. Insurance Co., 107 Ill. 652; Carey v. Mining Co., 81 Iowa, 674, 47 N. W. 882; Morrison v. Mining Co., 52 Cal. 306; Hawkins v. Mining Co., Id. 513.

⁵ Battelle v. Pavement Co., 37 Minn. 89, 33 N. W. 327.

⁶ Carmody v. Powers, 60 Mich. 26, 26 N. W. 801; Roberts Manuf'g Co. v. Schlick (Minn.) 64 N. W. 826; Hersey v. Tully (Colo. App.) 44 Pac. 854. As to the personal liability of promoters on contracts, see article by Henry O. Taylor, Esq., in 16 Am. Law Rev. 281.

⁷ Abbott v. Hapgood, 150 Mass. 248, 22 N. E. 907. Cf. Penn Match Co. v. Hapgood, 141 Mass. 145, 7 N. E. 22.

⁸ Kelner v. Baxter, L. R. 2 C. P. 174; Gunn v. Insurance Co., 12 O. B. (N. S.) 694; Melhado v. Railway Co., L. R. 9 C. P. 503; In re Empress Engineering Co., Clk.Pr.Corp.—8

within the scope of its general powers, may be adopted by the corporation after its organization, and thus become binding upon it, and binding in its favor on the other party.⁹ It is sometimes said that such contracts may be ratified by the corporation, but this is inaccurate, for ratification presupposes a principal existing at the time of the agent's action, whereas the corporation is not in existence at the time the contract is entered into by the promoter.¹⁰ The liability in case of adoption does not rest upon the idea of any supposed agency of the promoters, but upon the immediate and voluntary act of the company.¹¹ There is no difference between the making of a contract by a corporation by adoption of an agreement originally made in advance for it by promoters, and the making of an entirely new contract. No greater formality is required in the one case than in the other; and if it could make an entirely new contract without the use of its seal, or without writing, or without formal action of its board of directors, it may also so adopt an agreement made for it by its promoters. And it is not necessary that adoption of the agreement be express. It may be shown from acts or acquiescence of the corporation or its authorized agents, as any similar contract might be shown.¹² The contract in case of adoption is to be regarded as made by the corporation as of the date of the adoption, and not the date of the agreement by the promoter, and

16 Ch. Div. 125; *In re Northumberland Hotel Co.*, 33 Ch. Div. 16; *Spiller v. Skating Rink Co.*, 7 Ch. Div. 368.

⁹ *Battelle v. Pavement Co.*, 37 Minn. 89, 33 N. W. 327; *Whitney v. Wyman*, 101 U. S. 392; *Frankfort & S. T. Co. v. Churchill*, 6 T. B. Mon. 427; *Reichwald v. Hotel Co.*, 106 Ill. 439; *Buffington v. Bardon*, 80 Wis. 635, 50 N. W. 776; *Pittsburg & T. Copper Co. v. Quintrell*, 91 Tenn. 693, 20 S. W. 248; *McArthur v. Printing Co.*, 48 Minn. 319, 51 N. W. 216; *Grape Sugar & V. Manuf'g Co. v. Small*, 40 Md. 395; *Stanton v. Railway Co.*, 59 Conn. 272, 22 Atl. 300; *Little Rock & Ft. S. Ry. Co. v. Perry*, 37 Ark. 164; *Schreyer v. Mills Co. (Or.)* 43 Pac. 719; *Bommer v. Manufacturing Co.*, 81 N. Y. 468. See *Spiller v. Skating Rink Co.*, 7 Ch. Div. 368; *Mason v. Harris*, L. R. 11 Ch. Div. 97; 1 Cumming, Cas. Priv. Corp. 731.

¹⁰ *Weatherford, M. W. & N. W. Ry. Co. v. Granger*, 86 Tex. 350, 24 S. W. 795, *Shep. Cas. Corp.* 33; *McArthur v. Printing Co.*, 48 Minn. 319, 51 N. W. 216. Cf. *Stanton v. Railway Co.*, 59 Conn. 272, 22 Atl. 300.

¹¹ *Pittsburg & T. Copper Co. v. Quintrell*, 91 Tenn. 693, 20 S. W. 248.

¹² *Battelle v. Pavement Co.*, 37 Minn. 89, 33 N. W. 327; *Burden v. Burden*, 8 App. Div. 160, 40 N. Y. Supp. 499; *Schreyer v. Mills Co. (Or.)* 43 Pac. 719.

therefore a contract made by a promoter, and adopted by the corporation, is not within the statute of frauds, as not to be performed within a year, if it is to be performed within a year from such adoption, though not within a year from the date of the promoter's agreement.¹³

If a contract is made on behalf of a corporation by its promoters, and the corporation after its organization, and with knowledge of the facts, accepts its benefits, it must take them cum onere; and, if the contract has been performed by the other party, it may be enforced against the corporation. By accepting the benefits of the contract, the corporation adopts the contract.¹⁴ Thus, where a proposition was made on behalf of a railroad company by its promoters, that, if a bonus should be subscribed and paid to it, it would build a road between certain points, and would carry coal at a stipulated rate, it was held that the corporation, by accepting the bonus after its organization, adopted the contract, and was bound to fulfill the stipulations.¹⁵ In a Nebraska case, after articles of incorporation had been drawn up and signed by the promoters of a cattle company, but before they were filed, and before the time fixed in the articles for the commencement of business, a president was selected for the corporation by the promoters, and he, in their presence and with their approval, executed and delivered to a third person a note, purporting to be the note of the corporation, in payment for and in consideration of the sale and delivery of certain horses and cat-

¹³ *McArthur v. Printing Co.*, 48 Minn. 319, 51 N. W. 216.

¹⁴ *Weatherford, M. W. & N. W. Ry. Co. v. Granger*, 86 Tex. 350, 24 S. W. 795, *Shep. Cas. Corp.* 33; *Id.* (Tex. Civ. App.) 22 S. W. 70; *Battelle v. Pavement Co.*, 37 Minn. 89, 33 N. W. 327; *Moore & H. Hardware Co. v. Towers Hardware Co.*, 87 Ala. 206, 6 South. 41; *Paxton Cattle Co. v. First Nat. Bank*, 21 Neb. 621, 33 N. W. 271; *Grape Sugar & V. Manuf'g Co. v. Small*, 40 Md. 395; *Little Rock & Ft. S. Ry. Co. v. Perry*, 37 Ark. 164; *Schreyer v. Mill Co. (Or.)* 43 Pac. 719. And see *Rogers v. Land Co.*, 134 N. Y. 197, 32 N. E. 27; *Grand River Bridge Co. v. Rollins*, 13 Colo. 4, 21 Pac. 897. Cf. *Bell's Gap R. Co. v. Christy*, 79 Pa. St. 54, where the corporation was held not to be liable for services performed under an agreement with less than a majority of its promoters. And see, to the same effect, *Tift v. Bank*, 141 Pa. St. 550, 21 Atl. 660.

¹⁵ *Weatherford, M. W. & N. W. Ry. Co. v. Granger*, 86 Tex. 350, 24 S. W. 795, *Shep. Cas. Corp.* 33.

tle and a ranch and other property to the corporation. After the corporation was fully organized, and the time had arrived when it was authorized to commence business, the property came into its possession, and it continued to use and enjoy the same. It was held that this was an adoption of the note by the corporation, and that it was liable thereon.¹⁶

Where the promoters of a corporation have made a contract in its behalf, to be performed after it is organized, it may be deemed a continuing offer on the part of the other party to the agreement, like the offer in a subscription to the stock of a corporation to be formed in the future, and may be accepted and adopted by the corporation after its organization; and the exercise of any right inconsistent with the nonexistence of such contract ought to be deemed conclusive evidence of such acceptance or adoption, provided, of course, the corporation has knowledge of the facts.¹⁷

A distinction has been drawn, with respect to the rule that a corporation which accepts the benefits of a contract made by its promoters takes it cum onere, between a promise made on behalf of the corporation in the contract itself, the benefits of which the corporation has accepted, and a promise in a previous contract to pay for services in procuring the latter to be made; and it was held by the Texas supreme court that, while a corporation accepting a bonus contracted for by its promoters was bound by the stipulations in consideration of which the bonus was subscribed, it was not bound, by reason of its acceptance of the bonus, by a contract made by its promoters to pay a man for services in procuring subscribers to the bonus, since the latter contract was no part of the contract the benefits of which it accepted.¹⁸

To make a corporation liable for services performed under a contract with its promoters before its organization, the services must have been intended at the time to inure to the benefit of the future corporation, and must have been rendered in its behalf, and with

¹⁶ Paxton Cattle Co. v. First Nat. Bank, 21 Neb. 621, 33 N. W. 271.

¹⁷ Weatherford, M. W. & N. W. Ry. Co. v. Granger, 86 Tex. 350, 24 S. W. 795, Shep. Cas. Corp. 33.

¹⁸ Weatherford, M. W. & N. W. Ry. Co. v. Granger, 86 Tex. 350, 24 S. W. 795, Shep. Cas. Corp. 33, reversing Id. (Tex. Civ. App.) 23 S. W. 425.

the expectation that it would be bound. It will not be liable if they were rendered on the credit of the promoters individually.¹⁹

LIABILITY OF PROMOTERS TO CORPORATION AND STOCKHOLDERS.

48. Promoters, when acting for a projected corporation, occupy towards it a fiduciary relation, and for any secret profits made by them in transactions entered into on behalf of the corporation they may be compelled to account. This does not prevent a promoter from acquiring property on his own behalf, and selling it to the corporation, when organized, at an advance; and when he is not acting for the corporation, but merely as a vendor, he need not disclose his profits.

It is well settled that the promoters of a projected corporation occupy a fiduciary relation towards it, similar to that of an agent to a principal; and they have no right, in negotiations on behalf of the corporation, to derive any advantage over other stockholders without a full and fair disclosure of the transaction. Any secret profits made by them while acting for the corporation they must refund to it. The fact that there is no fraudulent intent on their part does not relieve them. Because of their position, the law forbids them to secretly derive any advantage over other stockholders, and makes them accountable for any profits realized by them.²⁰ And they may be made to account in a suit by the cor-

¹⁹ *Perry v. Railway Co.*, 44 Ark. 383. And see *Davis v. Creamery Co.* (Neb.) 67 N. W. 438.

²⁰ *Chandler v. Bacon*, 30 Fed. 538; *Woodbury Heights Land Co. v. Loudenslager* (N. J. Ch.) 35 Atl. 436; *Plaquemines Tropical Fruit Co. v. Buck*, 52 N. J. Eq. 219, 27 Atl. 1094; *Pittsburg Min. Co. v. Spooner*, 74 Wis. 307, 42 N. W. 259; *Simons v. Mining Co.*, 61 Pa. St. 202; *McElhenny's Appeal*, Id. 188; *Short v. Stevenson*, 63 Pa. St. 95; *Emery v. Parrott*, 107 Mass. 95; *Central Land Co. v. Obenchain*, 92 Va. 130, 22 S. E. 876; *Getty v. Devlin*, 54 N. Y. 403; *Yale Gas-Stove Co. v. Wilcox*, 64 Conn. 101, 29 Atl. 303; *Hichens v. Congreve*, 4 Russ. 562; *Bagnall v. Carlton*, 6 Ch. Div. 371; *Emma Silver Min. Co. v. Grant*, 11 Ch. Div. 918; *Burbank v. Dennis*, 101 Cal. 90, 35 Pac. 444; *Ex-Mission Land*

poration itself or its assignee or receiver;²¹ or the other stockholders may individually maintain an action for their proportion of such profits,²² or they may sue for damages in case for fraud.²³ A promoter, for instance, cannot purchase property, acting for the corporation, and then sell it to the corporation at an advance; nor can he negotiate a sale of property to the corporation, and secretly receive from the vendor a commission or bonus. In either case he will be compelled to account for the profits which he has realized.²⁴ In *Pittsburg Min. Co. v. Spooner*,²⁵ a complaint by a corporation for money alleged to have been received by the defendants to its use alleged, in substance, that the defendants, having obtained the right to purchase a certain mining option for \$20,000, proceeded to form the plaintiff corporation to make such purchase, representing to the persons who subscribed for stock that the option would cost \$90,000; and that, having first induced third persons to subscribe for the stock upon such representations, and to pay the corporation \$100,000 for their stock, the defendants then, as officers of the plaintiff corporation, purchased the option for it nominally for \$90,000, paying the \$20,000 which it actually cost them, with the money received from the sale of stock, and converting the remaining \$70,000 to their own use. It was held that the complaint stated a good cause of action in favor of the corporation.

This fiduciary relation exists between the promoter of a corporation and the corporation only where he is acting for the corporation.

& Water Co. v. Flash, 97 Cal. 610, 32 Pac. 600; *Gover's Case*, L. R. 20 Eq. 122; *Erlanger v. Phosphate Co.*, 3 App. Cas. 1218. Parties who act as agents for a corporation in acquiring property for it cannot make a profit out of the transaction; nor can they do so if they assume to act without precedent authority, if their transactions are accepted as the acts of agents by the corporation; and if, with a view to creating a corporation, persons represent themselves as acting for the company to be formed, and propose to sell at the prices they pay, and their purchases are taken on such representations, and stockholders invest thereon, it is a fraud on the company and interested parties to allow such agents to retain profits paid them in ignorance of the true sums actually advanced in making purchases. *Simons v. Mining Co.*, *supra*.

²¹ *Pittsburg Min. Co. v. Spooner*, *supra*; *Chandler v. Bacon*, *supra*.

²² *Emery v. Parrott*, *supra*; *Getty v. Devlin*, *supra*.

²³ *Getty v. Devlin*, *supra*.

²⁴ See the cases cited above.

²⁵ 74 Wis. 307, 42 N. W. 259.

There is no rule of law which prevents a promoter who owns property, though purchased by him for the purpose, from selling it to the corporation after it is organized. In such a case, in the absence of fraud, and if he is not acting also for the corporation, he may sell at such a price as he may be able to obtain from the board of directors, without regard to the original cost to him, and he is not bound to disclose the profits which he will realize by the transaction.²⁶ If the promoters who are selling property to a corporation are also the directors of the corporation, so that they also purchase for it, a different question arises. It is a case of the officers and agents of an existing corporation purchasing property for the corporation from themselves, and the most perfect good faith is required.²⁷

To constitute a person a promoter of a projected corporation, so as to bring him within the operation of this rule, it must affirmatively appear that he was acting for and in behalf of the proposed corporation, or that he assumed to so act.²⁸

²⁶ *Densmore Oil Co. v. Densmore*, 64 Pa. St. 43; *Lungren v. Pennell* (Pa. Sup.) 10 Wkly. Notes Cas. 297; *Ladywell Min. Co. v. Brookes*, 84 Ch. Div. 398; *Central Land Co. v. Obenchain*, 92 Va. 130, 22 S. E. 876; dictum in *Foss v. Harbottle*, 2 Hare, 461, 1 Cumming, Cas. Priv. Corp. 693. *Cl. Ex-Mission Land & Water Co. v. Flash*, 97 Cal. 610, 32 Pac. 600.

²⁷ Post, p. 508.

²⁸ *St. Louis, Ft. S. & W. R. Co. v. Tiernan*, 37 Kan. 606, 15 Pac. 544. One who engages with the owner of land in organizing a corporation to purchase it, by procuring subscriptions, and who frames the prospectus and becomes one of the first subscribers, is a promoter of the corporation. *Woodbury Heights Land Co. v. Loudenslager* (N. J. Ch.) 35 Atl. 436. And see other cases cited in note 18, *supra*.

CHAPTER V.

POWERS AND LIABILITIES OF CORPORATIONS.

- 49. In General.
- 50. Express Powers.
- 51. Powers Incidental to Corporate Existence.
- 52. Powers Implied from Powers Expressly Granted.
- 53. Construction of Charters—In General.
- 54. Power to Take and Hold Real and Personal Property.
- 55. Power to Act as Trustee.
- 56-57. Powers as to Contracts and Conveyances.
- 58-61. Form and Mode of Corporate Contracts.

IN GENERAL.

- 49. A corporation has such powers, and such powers only, as are conferred upon it by its charter. Powers may be conferred upon a corporation**
- (a) Expressly.**
 - (b) Impliedly, because they are incidental to corporate existence.**
 - (c) Impliedly, because they are necessary or proper in order to exercise the powers expressly conferred.**

A corporation, being a mere creature of the legislature, has such powers only as are conferred upon it by its charter. But it is not necessary that all powers, in order to exist, shall be conferred in express terms. It has, of course, all powers, expressly conferred, provided the legislature was not prevented from conferring them by some constitutional limitation. In addition to this, many powers are impliedly conferred or attach as being incidental to corporate existence, though not expressly mentioned in the charter. Again, the charter impliedly confers all powers, though not expressly mentioned, which are reasonably necessary and proper for the execution of the powers that are expressly conferred. "Corporations are creatures of the legislature, having no other powers than such as are given them by their charters, and such as are

incidental or necessary to carry into effect the purposes for which they were established.”¹

The rule in England is that a corporation has the same power to contract and act as a natural person has, except in so far as it may be restricted by its charter, expressly or impliedly. But it is also held that, when a corporation is created for a particular purpose, the act creating it impliedly prohibits it from exercising any powers not necessary or proper to carry out that purpose. It was said by Blackburn, J., in *Ashbury Railway Carriage & Iron Co. v. Riche*:² “I take it that the true rule of law is that a corporation at common law has, as an incident given by law, the same power to contract, and subject to the same restrictions, as a natural person has. And this is important when we come to construe the statutes creating a corporation, for if it were true that a corporation at common law has a capacity to contract to the extent given it by the instrument creating it, and no further, the question would be, does the statute creating the corporation by express provision or necessary implication show an intention in the legislature to confer upon this corporation capacity to make the contract? But if a body corporate has, as incident to it, a general capacity to contract, the question is, does the statute creating the corporation by express provision or necessary implication show an intention in the legislature to prohibit, and so avoid, the making of a contract of this particular kind?”³

In this country the general doctrine is that corporations organized under acts of the legislature have such powers, and such powers only, as are conferred, expressly or impliedly, by the acts. In *Thomas v. West Jersey R. Co.*⁴ it was insisted that a corporation “may do any act which is not either expressly or impliedly

¹ *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148, W. D. Smith, Cas. Corp. 129, Shep. Cas. Corp. 75; *Colman v. Railway Co.*, 10 Beav. 1, 1 Cumming, Cas. Priv. Corp. 136; *Thomas v. Railroad Co.*, 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164, W. D. Smith, Cas. Corp. 132, Shep. Cas. Corp. 70; *Byrne v. Manufacturing Co.*, 65 Conn. 336, 81 Atl. 833.

² L. R. 9 Exch. 224, 2 Cumming, Cas. Priv. Corp. 34.

³ *South Yorkshire Ry. & River Dun Co. v. Great Northern Ry. Co.*, 9 Exch. 84.

⁴ 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164.

prohibited by its charter, although, where the act is unauthorized by the charter, a shareholder may enjoin its execution, and the state may, by proper process, forfeit the charter." The court, however, did not take this view, but said: "We take the general doctrine to be in this country, though there may be exceptional cases and some authorities to the contrary, that the powers of corporations organized under legislative statutes are such, and such only, as those statutes confer. Conceding the rule applicable to all statutes, that what is fairly implied is as much granted as what is expressed, it remains that the charter of a corporation is the measure of its powers, and that the enumeration of these powers implies the exclusion of all others."

EXPRESS POWERS.

50. A corporation has all powers expressly conferred upon it by its charter, unless conferred in violation of constitutional limitations.

Of the powers expressly conferred upon a corporation, there is little to be said. The questions which arise in this connection are chiefly questions of construction. The legislature has the absolute power to confer upon a corporation any power it may see fit to confer, so long as it does not violate any limitation contained in the state or federal constitution. A grant of powers in violation of constitutional limitations can have no effect.

POWERS INCIDENTAL TO CORPORATE EXISTENCE.

51. Certain powers are incidental to corporate existence, and are impliedly conferred upon every corporation unless there is something to show an intention to exclude them. These powers are:

- (a) To have perpetual or continuous succession during the period for which it is created. It therefore has the power to elect members in the place of those removed by death or otherwise.**
- (b) To have a corporate name, and to contract, to grant and receive, and to sue and be sued thereby.**

- (c) To purchase and hold real and personal property for purposes authorized by its charter.
- (d) To have a common seal.
- (e) To make by-laws for its government.
- (f) The power of motion or removal of members. But this power is not incident to a joint-stock corporation.

When a corporation is created, certain powers are impliedly attached to it as incidental to its existence, though not expressly mentioned in the charter. These powers are: (1) To have perpetual or continuous succession; (2) to have a corporate name, and to contract, to grant and receive, and to sue and be sued thereby; (3) to purchase and hold real and personal property for purposes authorized by its charter; (4) to have a common seal; (5) to make by-laws; (6) the power of motion, or removal of members, in the case of corporations other than joint-stock corporations.⁵ Some of these powers, as has been seen,⁶ are essential to corporate existence, while others are incidental, but not essential, and may be withheld.

As we have seen in a former chapter, the power of perpetual succession, or succession during the period for which it is created, is not only an incident which attaches to every corporation, but is essential to corporate existence. A corporation, therefore, has the implied power to elect members in the place of those who are removed by death or otherwise.⁷

So with the power to have a corporate name, and to contract obligations, receive and grant, and sue and be sued thereby. This power attaches as incidental to corporate existence. The power to contract is restricted to purposes authorized by the charter.⁸

The power to purchase and hold real or personal property is incidental to corporations, but not essential. This power, like the power to contract, is limited to purposes authorized by the charter.⁹

⁵ 2 Kent, Comm. 277, 278.

⁶ Ante, p. 12.

⁷ 1 Bl. Comm. 475.

⁸ Ante, pp. 17, 71; post, pp. 133-156.

⁹ Post, p. 128.

The power to have a common seal, though not essential to corporate existence, is an incident which attaches to every corporation without express provision. The necessity to use a seal will be considered in another place.¹⁰

Every corporation has the implied power to make by-laws for its government, but this power is not essential. It may be dispensed with if the charter sufficiently provides for the government of the body. This power will be considered at length in a subsequent chapter.¹¹

The power of motion, or removal of members, is said to be incident to corporations; and this is true of many corporations, like boards of trade, and other non-stock corporations; but no such power is incident to modern joint-stock corporations. This power will be further discussed in treating of the relation between the corporation and its members.¹²

POWERS IMPLIED FROM POWERS EXPRESSLY GRANTED.

52. All powers that are reasonably necessary or proper for the execution of the powers expressly granted, and that are not expressly or impliedly excluded, are impliedly conferred.

Corporations not only have the powers expressly granted by the charter, and the particular powers which have been mentioned as incidental to corporate existence, but, in addition, they have all powers that are reasonably necessary or proper for the execution of the powers that are expressly granted, provided such powers are not withheld.

CONSTRUCTION OF CHARTERS—IN GENERAL.

53. In the construction of charters the intention of the legislature must be ascertained, and must govern. The rules are substantially the same as in the case of

¹⁰ Post, p. 156.

¹¹ Post, p. 454.

¹² Post, p. 401.

other statutes. The following rules may be particularly mentioned:

- (a) In cases of doubt, charters are to be construed most strongly in favor of the public, and against the corporation. Some of the courts limit this rule to cases where the corporation claims powers in derogation of common right.
- (b) Where general words follow an enumeration of persons or things by words of particular and specific meaning, such general words are not to be construed in their widest sense, unless such seems clearly to have been the intention of the legislature, but are to be held as applying only to persons or things of the same general kind or class as those specifically mentioned.
- (c) If a charter expressly enumerates certain powers, this impliedly excludes all other powers except those mentioned, and such as may be necessary or proper to the execution of them.

When a corporation is formed under a special act, its powers are generally specified in the act, and the act, together with any other laws which are binding upon it, constitute its charter. When a corporation is formed under a general law, this law, together with the articles of association required by the law to be executed and filed by the incorporators, and any other laws of the state which are applicable to such corporations, constitute its charter.¹⁸

Construction in Favor of the Public in Case of Doubt.

In the construction of contracts between individuals it is a rule that the language must be taken most favorably, in case of doubt, against the party using it. The rule for construing corporate charters is different. It has often been held that charters secured under special legislative grants will, in case of doubt, be construed most strongly against the grantees and in favor of the public. As was said by an English judge: "The language of these acts * * * is to

¹⁸ *Lincoln Shoe Manuf'g Co. v. Sheldon*, 44 Neb. 279, 62 N. W. 480.

be treated as the language of the promoters of them. They ask the legislature to confer great privileges upon them, and profess to give the public certain advantages in return. Acts passed under such circumstances should be construed strictly against the parties obtaining them, but liberally in favor of the public."¹⁴ The same rule applies to the construction of the charters of corporations formed under general laws. "In the construction of a charter, to be in doubt is to be resolved, and every resolution which springs from doubt is against the corporation, and in favor of the public."¹⁵

This rule applies only in cases of doubt. The intention of the legislature must be ascertained, and must govern. Unless there is doubt, the language of the charter must be given effect. Some of the courts limit the rule that charters are to be construed, in cases of doubt, most strongly against the corporation, to cases in which the corporation claims powers in derogation of common right, as the power of eminent domain. "In giving a construction to the powers of a corporation," it has been said, "the language of the charter should in general neither be construed strictly nor liberally, but according to the fair and natural import of it, with reference to the purposes and objects of the corporation. If the powers conferred are against common right, and trench in any way upon the privileges of other citizens, they are, in cases of doubt, to be construed strictly,

¹⁴ *Parker v. Railway Co.*, 7 Man. & G. 288. And see, to the same effect, *State v. Payne*, 129 Mo. 468, 31 S. W. 797; *Stourbridge Canal Co. v. Wheeley*, 2 Barn. & Adol. 792, 1 Cumming, Cas. Priv. Corp. 298; *Charles River Bridge v. Warren Bridge*, 11 Pet. 420, 1 Cumming, Cas. Priv. Corp. 506; *The Binghamton Bridge*, 3 Wall. 51; *Parrot v. Lawrence*, 2 Dill. 332, Fed. Cas. No. 10,772; *Northwestern Fertilizing Co. v. Village of Hyde Park*, 97 U. S. 659; *Mills v. County of St. Clair*, 8 How. 569; *Com. v. Erie & N. E. R. Co.*, 27 Pa. St. 339; *Ross-Meehan B. S. F. Co. v. Southern M. Iron Co.*, 72 Fed. 957. In a leading English case, where the question was whether certain powers were impliedly granted in the charter of a canal company, the court said: "The canal having been made under an act of parliament, the rights of the plaintiffs are derived entirely from that act. This, like many other cases, is a bargain between a company of adventurers and the public, the terms of which are expressed in the statute; and the rule of construction in all such cases is now fully established to be this; that any ambiguity in the terms of the contract must operate against the adventurers, and in favor of the public, and the plaintiffs can claim nothing that is not clearly given them by the act." *Stourbridge Canal Co. v. Wheeley*, *supra*.

¹⁵ *Black v. Canal Co.*, 24 N. J. Eq. 474.

but not so as to impair or defeat the objects of the incorporation.”¹⁶

Powers and privileges in derogation of common right, or such as are not common to individuals, will never be implied, but must be expressly conferred. As was said by Chief Justice Marshall: “The great object of an incorporation is to bestow the character and properties of individuality on a collected and changing body of men. Any privileges which may exempt them from the burdens common to individuals do not flow necessarily from the charter, but must be expressed in it, or they do not exist.”¹⁷

General Terms Following Special Terms.

The rule of statutory construction, “that, where general words follow an enumeration of persons or things by words of particular and specific meaning, such general words are not to be construed in their widest extent, but are to be held as applying only to persons or things of the same general kind or class as those specifically mentioned,”¹⁸ applies, of course, to the construction of charters. Thus, where a corporation was authorized by its charter “to carry on the business of mechanical engineers and general contractors,” it was held that the term “general contractors” would be referred to that which was immediately before, and authorized such contracts only as mechanical engineers were in the habit of making.¹⁹ In construing charters, as in construing other statutes, the intention of the legislature must always govern. Therefore, this rule must be disregarded where the legislative intention is plain to the contrary.²⁰

¹⁶ *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148. And see *Whitaker v. Canal Co.*, 87 Pa. St. 34.

¹⁷ *Providence Bank v. Billings*, 4 Pet. 514.

¹⁸ Black, *Interp. Laws*, 141.

¹⁹ *Directors, etc., of Ashbury Railway Carriage & Iron Co. v. Riche*, L. R. 7 H. L. 653, 1 Cumming, Cas. Priv. Corp. 152. So, where the charter of a corporation authorized it “to purchase, lease, work, and sell mines, minerals, land, and buildings,” the general words “land and buildings” were limited to land and buildings acquired for the purpose of purchasing, leasing, working or selling of mines and minerals. *Directors, etc., of Ashbury Railway Carriage & Iron Co. v. Riche*, *supra*. There are many cases in which this rule of construction has been applied. See ante, p. 69, where some of the cases are referred to.

²⁰ Black, *Interp. Laws*, 141, 143; ante, p. 69.

Express Mention and Implied Exclusion.

The general rule of statutory construction, that the express mention of one thing is tantamount to an exclusion of all others, applies to the construction of charters.²¹ Therefore, if a charter expressly enumerates certain powers, this impliedly excludes all other powers except those mentioned, and such as may be necessary or proper to the execution of them. If, for instance, the charter of a corporation enumerates the purposes for which it may acquire and hold lands, it cannot acquire and hold land for any other purpose.²² So, if a corporation is expressly authorized to lend money on bond and mortgage, it cannot lend on any other security.²³ And a bank authorized to do a banking business "by discounting" notes cannot buy them.²⁴

**POWER TO TAKE AND HOLD REAL AND PERSONAL
PROPERTY.**

54. In the absence of express restrictions in its charter or in some statute applicable to it, a corporation has the implied power to take and hold property, real or personal, by purchase, gift, devise or bequest. But—

- (a) It cannot acquire or hold property for a purpose that is foreign to the objects for which it was created.
- (b) In some jurisdictions there are statutory limitations on its power to take by devise.

The power to purchase and hold such real and personal property as the purposes of the corporation may render necessary or proper is incident, at common law, to all corporations, unless they are specially restrained by their charter or by some statute. Such power is generally expressly conferred by the charter; but it is not at all necessary that it should be, for it is always implied, in the absence of ex-

²¹ Black, *Interp. Laws*, 146; *Farmers' & Mechanics' Bank v. Baldwin*, 28 Minn. 198; *Case v. Kelly*, 133 U. S. 21, 10 Sup. Ct. 216, 1 Cumming, *Cas. Priv. Corp.* 106, *Shep. Cas. Corp.* 102; *Talmage v. Pell*, 7 N. Y. 328.

²² *Case v. Kelly*, 133 U. S. 21, 10 Sup. Ct. 216, 1 Cumming, *Cas. Priv. Corp.* 106, *Shep. Cas. Corp.* 102.

²³ *Life & Fire Ins. Co. v. Mechanic Fire Ins. Co.*, 7 Wend. (N. Y.) 81.

²⁴ *Farmers' & Mechanics' Bank v. Baldwin*, 28 Minn. 198; *post*, p. 141.

press restriction.²⁵ And subject to the same limitations, it may take by gift, bequest, or devise.²⁶ As we shall presently see at some length, it cannot purchase property for a purpose not authorized by its charter.²⁷ Nor has it any right to take property, either real or personal, by gift, bequest, or devise, for an unauthorized purpose.²⁸ Where a charter enumerates the purposes for which the corporation may acquire and hold real estate, it impliedly excludes all other purposes.²⁹ Therefore, where the charter of a railroad company authorized it to take lands for a right of way, and for certain enumerated purposes connected with the use and management of the road, it was held that it could not take lands by donation not for use in connection with the road.³⁰ In some states the amount or value of property which particular corporations may take is limited by charter or by statute. Such a restriction only applies to the value of the property at the time it is acquired, and a subsequent rise in value does not require the corporation to dispose of part of it, or affect its title.³¹ A corporation is presumed, in the absence of evidence to the contrary, to have the right to purchase and hold real estate.³²

By the English statutes of mortmain, corporations were prohibited from purchasing lands without license from the king, but these statutes, except in Pennsylvania, were not adopted in this country,

²⁵ Co. Litt. 44c, 800b; 2 Kent, Comm. 281; *Nicoll v. Railroad Co.*, 12 N. Y. 121, 1 Cumming, Cas. Priv. Corp. 73; *Regents of University of Michigan v. Detroit Young Men's Soc.*, 12 Mich. 138; *Blanchard's Gun-Stock Turning Factory v. Warner*, 1 Blatchf. 258, Fed. Cas. No. 1,521; *Lathrop v. Bank*, 8 Dana (Ky.) 114; *Thompson v. Waters*, 25 Mich. 214; *Rivanna Nav. Co. v. Dawsons*, 8 Grat. (Va.) 19. Where a corporation is legally organized for the specific purpose of dealing in land, its power to hold land is not limited. *Market St. Ry. Co. v. Hellman*, 109 Cal. 571, 42 Pac. 225.

²⁶ Cases above cited. As to devise, see post, p. 131.

²⁷ Post, p. 140.

²⁸ *Case v. Kelly*, 133 U. S. 21, 10 Sup. Ct. 216, 1 Cumming, Cas. Priv. Corp. 106, Shep. Cas. Corp. 102.

²⁹ Ante, p. 128.

³⁰ *Case v. Kelly*, 133 U. S. 21, 10 Sup. Ct. 216, 1 Cumming, Cas. Priv. Corp. 106, Shep. Cas. Corp. 102.

³¹ 2 Inst. 722; *Bogardus v. Trinity Church*, 4 Sandf. Ch. (N. Y.) 633.

³² *People v. La Rue*, 67 Cal. 526, 8 Pac. 84; *Stockton Sav. Bank v. Staples*, 98 Cal. 189, 32 Pac. 936.

and did not become a part of our law.⁸³ They have been recognized as in force in Pennsylvania so far as applicable to its conditions, and as having the effect of rendering void all conveyances or devises of land to or for the use of a corporation, unless sanctioned by its charter or by act of the legislature.⁸⁴ Even in Pennsylvania, however, it has been held by the United States supreme court that a conveyance of land to a corporation without legislative sanction vests the title in the corporation, subject to forfeiture at the instance of the commonwealth only.⁸⁵

A corporation is not prevented from taking a grant of land in fee by the fact that its period of existence is limited to a term of years. Such a corporation may take a fee-simple title, and may sell the land whenever it is no longer necessary or convenient, though it could not hold and enjoy the same after the expiration of its charter.⁸⁶ "Corporations have a fee simple for the purpose of alienation, but they have only a determinable fee for the purpose of enjoyment. On the dissolution of the corporation, the reverter is to the original grantor or his heirs; but the grantor will be excluded by the alienation in fee, and in that way the corporation may defeat the possibility of a reverter."⁸⁷ Where a corporation acquires title to land in fee simple, the land does not revert to the grantor or his heirs on abandonment of its use for corporate purposes, unless it is so provided in the charter or in some statute.⁸⁸

At common law, none but natural persons can take in joint tenancy. A corporation cannot take such an estate, either jointly with another corporation or with a natural person. The reason assigned by the early writers is that they hold in different capacities and in dif-

⁸³ 2 Kent, Comm. 281-283; *Rivanna Nav. Co. v. Dawsons*, 3 Grat. (Va.) 19; *Fayette Land Co. v. Louisville & N. R. Co.* (Va.) 24 S. E. 1016; *Moore's Heirs v. Moore's Devisees*, 4 Dana (Ky.) 354; *Lathrop v. Bank*, 8 Dana (Ky.) 114; *Page v. Heineberg*, 40 Vt. 81, 1 Cumming, Cas. Priv. Corp. 76.

⁸⁴ *Methodist Church v. Remington*, 1 Watts (Pa.) 218.

⁸⁵ *Runyan v. Coster's Lessee*, 14 Pet. 122.

⁸⁶ *Nicoll v. Railroad Co.*, 12 N. Y. 121, 1 Cumming, Cas. Priv. Corp. 73; *People v. Mauran*, 5 Denio (N. Y.) 389; *Page v. Heineberg*, 40 Vt. 81, 1 Cumming, Cas. Priv. Corp. 76; *Rives v. Dudley*, 3 Jones, Eq. (N. C.) 126.

⁸⁷ 2 Kent, Comm. 282.

⁸⁸ *Page v. Heineberg*, 40 Vt. 81, 1 Cumming, Cas. Priv. Corp. 76.

ferent rights.³⁹ There is nothing, however, to prevent a corporation and a natural person, or two corporations, from holding as tenants in common.⁴⁰

Power to Take by Devise.

By the English statute of wills passed in the time of Henry VIII., corporations were not allowed to take real estate by will; and in some of our states the statute of wills prohibits devises to a corporation, unless it be expressly authorized by its charter or by statute to take by devise.⁴¹ In the absence of such a restriction in a statute, or in the charter of a corporation, it may take real estate by devise as well as by purchase.⁴² If the charter of a corporation prohibits it from taking by devise, it cannot take in another state, though there may be no prohibitory statute in the latter state, for a prohibitory clause in the charter of a corporation cleaves to it everywhere; but it has been held that a statute of wills of one state, since it has no extraterritorial effect, cannot prevent a corporation of that state from taking by devise in another state, where there is no such prohibition.⁴³

It seems that the statute of wills, in prohibiting a devise to a corporation, does not render invalid a devise to a natural person in trust

³⁹ Telfair v. Howe, 3 Rich. Eq. (S. C.) 235.

⁴⁰ See New York & S. Canal Co. v. Fulton Bank, 7 Wend. (N. Y.) 412, 2 Cumming, Cas. Priv. Corp. 87.

⁴¹ See McCartee v. Society, 9 Cow. (N. Y.) 437; Downing v. Marshall, 23 N. Y. 366; Starkweather v. Society, 72 Ill. 50. Such a provision does not prevent a corporation from taking money under a will, though raised by a conversion of land under a power in the will. Downing v. Marshall, supra. But where real estate itself is devised to a corporation, which is incapable of taking real estate in that way, a court of equity has no power to convert it into money, and direct the payment of the money to it. Such direction must appear in the will. Starkweather v. Society, supra. A devise to a corporation not authorized to take land by devise is not made valid by amendment of its charter after the testator's death. White v. Howard, 46 N. Y. 144.

⁴² White v. Howard, 38 Conn. 342, 1 Cumming, Cas. Priv. Corp. 81. Rivanna Nav. Co. v. Dawson, 3 Grat. (Va.) 19. Moore's Heirs v. Moore's Devisees, 4 Dana (Ky.) 354.

⁴³ White v. Howard, supra. Contra, Starkweather v. Society, 72 Ill. 50. But where the laws of a state prohibit a corporation from taking by devise, a devise to a foreign corporation is void, though by its charter it is authorized to take by devise. White v. Howard, 46 N. Y. 144.

to apply the rents and profits for the use and benefit of a corporation, as the devise in such a case is not to the corporation, but to the trustee; but on this point there is some doubt, and the contrary has been held under the New York statute.⁴⁴

Power to Take Mortgage.

If a corporation is authorized to engage in a transaction by which a third person becomes indebted to it, it has the implied power, in the absence of prohibition in its charter, to take a mortgage on real estate to secure the debt; and such a transaction is not within a prohibition against dealing in lands.⁴⁵

POWER TO ACT AS TRUSTEE.

55. A corporation having power to take and hold property has the capacity to take and hold the same in trust, and to execute the trust, if the trust is not repugnant to the purposes for which it was created. In the latter case, the trust, if otherwise good, is not void, but a court of equity will appoint a new trustee to execute it.

It was at one time considered that a corporation aggregate had no capacity to act as trustee, executor, guardian, etc. The reason given by Blackstone why it could not act as executor or administrator was that it could not take the necessary oath. Another reason why it could not act as trustee, which was often assigned, was that a court of equity sometimes enforced a trust by laying hold of the conscience of the trustee, and a corporation aggregate had no conscience. The reason most commonly given was that appointment as trustee involved a personal trust, and therefore a corporation lacked one of the essential requisites of a good trustee,—personal confidence. These reasons are all artificial and without weight, and the old doctrine which was based upon them has been exploded and repudiated; and it is now well settled that a corporation, if authorized by its charter, as in the case of modern trust companies, hospitals,

⁴⁴ *McCartee v. Society*, 9 Cow. (N. Y.) 437; *Downing v. Marshall*, 23 N. Y. 366.

⁴⁵ *Blunt v. Walker*, 11 Wis. 334.

universities, etc., may act as a trustee to the same extent as a natural person.⁴⁶ Statutes have been enacted, in many states, authorizing the formation of corporations with the power to act as trustee, executor, administrator, or guardian, and such statutes have been held valid.⁴⁷ Independently of any statute, where a corporation has the power to take real and personal property by conveyance and by devise, it may also so take and hold property in trust in the same manner, and to the same extent, as a natural person may. If the trust is repugnant to, or inconsistent with, the purpose for which the corporation was created, it cannot be compelled to execute the trust; but the trust, if otherwise unexceptionable, will not be void, and a court of equity will appoint a new trustee to carry out its objects.⁴⁸ If property is conveyed, bequeathed, or devised to a corporation in trust, and the trusts are in themselves valid, but the corporation, by reason of its purpose, is incompetent to execute them, the heirs of the grantor or testator cannot take advantage of such inability. The objection can be raised only by the state in its sovereign capacity, by a quo warranto or other proper judicial proceeding.⁴⁹

POWERS AS TO CONTRACTS AND CONVEYANCES.

56. A corporation has no power to enter into any contract that is not expressly or impliedly authorized by its charter. But any contract that is reasonably necessary or proper for carrying out the powers expressly conferred is impliedly authorized. Among the powers impliedly conferred upon every corporation, in the absence of express restrictions in its charter, are the following:

(a) A corporation has the implied power to purchase such real and personal property as its purposes

⁴⁶ *Vidal v. Mayor, etc.*, 2 How. 127, 183; *Trustees of Phillip's Academy v. King*, 12 Mass. 546; *Chambers v. City of St. Louis*, 29 Mo. 543; *Minnesota Loan & Trust Co. v. Beebe*, 40 Minn. 7, 41 N. W. 232.

⁴⁷ *Minnesota Loan & Trust Co. v. Beebe*, 40 Minn. 7, 41 N. W. 232.

⁴⁸ *Vidal v. Mayor, etc.*, 2 How. 127, 183.

⁴⁹ *Id.*

may require; but it has no power to purchase property for a purpose foreign to the objects for which it was created.

- (b) A corporation generally has the implied power to sell and convey or mortgage real or personal property owned by it. But a railroad company, or other quasi public corporation, cannot dispose of or mortgage property which is needed in order to carry on the business for which it was created, unless expressly authorized. Nor can a corporation transfer or mortgage its franchise without statutory authority.
- (c) It has the power to borrow money whenever the nature of its business renders it proper or expedient.
- (d) It has the power to execute a bond for any purpose for which it may contract a debt.
- (e) In this country, but not in England, it has the power to make or indorse promissory notes, and to draw, indorse, or accept bills of exchange, if it is a usual or proper means of accomplishing the objects for which it was created.
- (f) Subject to certain exceptions, it has no power to enter into a contract of suretyship or guaranty unless the power is expressly conferred. And it cannot bind itself by an accommodation note or bill.
- (g) It has no implied power to enter into a contract of partnership. But it may contract jointly with another.
- (h) Though there are some cases to the contrary, by the better opinion a corporation has no power, unless expressly authorized, to subscribe for, purchase, or hold stock in another corporation. But it may in good faith take and hold stock in another corporation to secure a loan previously made by it, or a debt due it, or in payment of such loan or debt.

(i) In some jurisdictions it is held that a corporation has no implied power to purchase its own stock, either for the purpose of selling or reissuing it, or for the purpose of holding or retiring it, though it may take its own stock to secure a loan previously made or a debt due it, or in payment of such loan or debt. In other jurisdictions it may thus purchase its own stock, subject to the rights of creditors.

57. The presumption is that contracts of a corporation are within its powers, and the burden of showing the contrary rests upon the party who objects.

Since a corporation has such powers only as are expressly or impliedly conferred upon it, by its charter, it follows that it cannot legally enter into any contract that is not expressly or impliedly authorized.⁵⁰ A contract in excess of its powers is said to be *ultra vires*. Whether it is void or not is a question upon which the courts do not agree. We shall consider the effect of *ultra vires* contracts in a subsequent chapter. As a rule, so long as the contract is executory, it cannot be enforced. The fact that the particular contract may be, or is even sure to be, profitable to the corporation by greatly increasing its business or its property, is altogether immaterial.⁵¹ Nor can it make any difference that there is nothing illegal about

⁵⁰ *Coleman v. Railway Co.*, 10 Beav. 1, 1 Cumming, Cas. Priv. Corp. 136; *East Anglian Rys. Co. v. Eastern Counties Ry. Co.*, 11 C. B. 775, 1 Cumming, Cas. Priv. Corp. 142; *Franklin Co. v. Lewiston Inst. for Savings*, 68 Me. 43, 1 Cumming, Cas. Priv. Corp. 343; *Pearce v. Railroad Co.*, 21 How. 441, 1 Cumming, Cas. Priv. Corp. 146; *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148; *W. D. Smith, Cas. Corp.* 129, *Shep. Cas. Corp.* 75; *Directors, etc., of Ashbury Railway Carriage & Iron Co. v. Riche*, L. R. 7 H. L. 653; 1 Cumming, Cas. Priv. Corp. 152; *Thomas v. Railroad Co.*, 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164; *W. D. Smith, Cas. Corp.* 132, *Shep. Cas. Corp.* 70; *Davis v. Railroad Co.*, 131 Mass. 258, 1 Cumming, Cas. Priv. Corp. 173; *Weckler v. Bank*, 42 Md. 581; *Chewacla Lime Works v. Dismukes*, 87 Ala. 344, 6 South. 122; *Tomkinson v. Railway Co.*, 35 Ch. Div. 675.

⁵¹ *Coleman v. Railway Co.*, 10 Beav. 1, 1 Cumming, Cas. Priv. Corp. 136; *Davis v. Railroad Co.*, 131 Mass. 258, 1 Cumming, Cas. Priv. Corp. 173; *Tomkinson v. Railway Co.*, 35 Ch. Div. 675; and the other cases cited above.

the subject-matter of the contract. It is unauthorized, and that is enough.

It has been held, for instance, that a railroad company, which has been given the power only to construct, maintain, and operate a certain railroad, and to do all that may be necessary for the purpose of carrying on and working the road, has no power to pledge its funds for the purpose of supporting or aiding in the support of another corporation to operate a connecting steamboat line, however much such an arrangement may increase the traffic on the railroad.⁵² So, it has been held that a railroad company has no implied power to purchase and operate a steamboat, at least on waters at the terminus of its line, or at any other place where a steamboat is not necessary to the operation of the road;⁵³ or to lease and operate another railroad;⁵⁴ or to lease or transfer its own road to another corporation or person;⁵⁵ or to enter into a consolidation agreement with another railroad corporation;⁵⁶ or to lease or transfer to another a telegraph line which it has constructed and is operating under its charter.⁵⁷

So, where a corporation was empowered to lay out and maintain a road from some point in the vicinity of Mt. Washington to the top

⁵² *Coleman v. Railway Co.*, 10 Beav. 1, 1 Cumming, Cas. Priv. Corp. 136. But see *Green Bay & M. R. Co. v. Union Steamboat Co.*, 107 U. S. 98, 2 Sup. Ct. 221.

⁵³ *Pearce v. Railroad Co.*, 21 How. 441, 1 Cumming, Cas. Priv. Corp. 146; *Central Railroad & Banking Co. v. Smith*, 76 Ala. 572. It would doubtless be different if a corporation were chartered to construct and operate a railroad along a route crossing a wide river, or under other circumstances rendering transportation by water necessary to the operation of the road.

⁵⁴ *East Anglian Ry. Co. v. Eastern Counties Ry. Co.*, 11 O. B. 775, 1 Cumming, Cas. Priv. Corp. 142.

⁵⁵ *Thomas v. Railroad Co.*, 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164, W. D. Smith, Cas. Corp. 132, Shep. Cas. Corp. 70; *New York & M. L. R. Co. v. Winans*, 17 How. (U. S.) 30; *Pennsylvania R. Co. v. St. Louis, A. & T. H. R. Co.*, 118 U. S. 290, 6 Sup. Ct. 1094, and 7 Sup. Ct. 24; *Black v. Canal Co.*, 22 N. J. Eq. 390; *Central Transp. Co. v. Pullman's Palace-Car Co.*, 139 U. S. 24, 11 Sup. Ct. 478; *Oregon Ry. & Nav. Co. v. Oregonian Ry. Co.*, 130 U. S. 1, 9 Sup. Ct. 409; post, p. 142.

⁵⁶ *Pearce v. Railroad Co.*, 21 How. (U. S.) 441, 1 Cumming, Cas. Priv. Corp. 146; *Clearwater v. Meredith*, 1 Wall. (U. S.) 25.

⁵⁷ *American Union Tel. Co. v. Union Pac. Ry. Co.*, 1 McCrary, 188, 1 Fed. 745, 1 Cumming, Cas. Priv. Corp. 284; post, p. 142.

of the mountain, to take tolls of passengers and for carriages, to build and own tollhouses, and to take land for their road, it was held that the corporation had no power to purchase omnibuses, wagons, horses, etc., and engage in the carriage of passengers and their baggage on its road.⁵⁸ And a manufacturing corporation authorized to engage in the manufacture of firearms and other implements of war cannot engage in the manufacture of railroad locks.⁵⁹

It has been held that a railroad, manufacturing, banking, or other business corporation cannot enter into a valid contract to pay money to defray the expenses of holding a festival or carnival, though by bringing strangers into the place their business may be greatly increased.⁶⁰ This, however, is very doubtful, and there are decisions to the contrary.⁶¹ We shall presently see more at length that, as a rule, a corporation, unless expressly authorized, has no power to become surety or guarantor for another, or to enter into a contract of partnership, or to deal in stock of another corporation. To these rules, however, as we shall see, there are some exceptions.⁶² Other illustrations are given below.⁶³

⁵⁸ *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148, W. D. Smith, Cas. Corp. 129, Shep. Cas. Corp. 75.

⁵⁹ *Whitney Arms Co. v. Barlow*, 63 N. Y. 62, 1 Cumming, Cas. Priv. Corp. 253. So, a corporation for the purpose of manufacturing and dealing in metal goods cannot contract with another company, engaged in manufacturing carbons for electric lighting, to sell its carbons for a term of years. *Holmes, Booth & Haydens v. Willard*, 125 N. Y. 75, 25 N. E. 1083.

⁶⁰ *Davis v. Railroad Co.*, 131 Mass. 258, 1 Cumming, Cas. Priv. Corp. 173. And see *Tomkinson v. Railway Co.*, 35 Ch. Div. 675.

⁶¹ In *Richelleu Hotel Co. v. International Military Encampment Co.*, 140 Ill. 248, 29 N. E. 1044, however, it was held that a subscription by an hotel company to a fund to establish a military encampment, which would be likely to attract strangers, necessarily requiring hotel accommodations, was not ultra vires. So, it has been held by the Illinois court that a business corporation may subscribe money in consideration of securing the location of a post office near its place of business. *B. S. Green Co. v. Blodgett*, 159 Ill. 169, 42 N. E. 176, affirming 55 Ill. App. 556. And in *Temple Street Cable Ry. Co. v. Hellman*, 103 Cal. 634, 37 Pac. 530, the giving of its note by a street-railroad company, as an inducement to the establishment of a baseball park, which would increase its traffic, was sustained against an attack upon it as ultra vires.

⁶² Post, pp. 148-155.

⁶³ National banks have no authority to sell railroad bonds on commission. *Weckler v. Bank*, 42 Md. 581. A railroad corporation cannot engage in banking, as by issuing paper designed to circulate as bank notes, or deal in notes and

Powers Impliedly Conferred.

As has been stated generally in a former section, power to enter into a particular contract need not be expressly conferred. On the contrary, the power to make all such contracts as are necessary and usual in the course of business, or are reasonably incident to the objects for which the corporation was created, is always implied, where there is no positive restriction in the charter.⁶⁴ "When a charter or act of incorporation and valid statutory law are silent as to what contracts a corporation may make, as a general rule it has power to make all such contracts as are necessary and usual in the course of business, as means to enable it to attain the object for which it was created, and none other. The creation of a corporation for a specific purpose implies a power to use the necessary and usual means to effectuate that purpose."⁶⁵

Thus, a corporation, unless restricted by its charter, has the implied power to lease or mortgage property lawfully held by it under

bills. *People v. River Raisin & L. E. R. Co.*, 12 Mich. 389; *Goodrich v. Reynolds*, 31 Ill. 490. In *Byrne v. Manufacturing Co.*, 65 Conn. 336, 31 Atl. 833, the officers of an insolvent corporation, for the purpose of avoiding dissolution, transferred all its property to another corporation, which had been organized to continue its business, and accepted, in payment, stock in the new corporation, to be held by trustees named by such officers. The contract was held ultra vires. A railroad corporation has no power to employ a person to make a report on mines of which its road is the outlet, though its business is benefited thereby. *Georg v. Railroad Co.* (Nev.) 38 Pac. 441. A corporation authorized by its charter to make contracts of fire and marine insurance, to loan money on bottomry, respondentia, or mortgage, to buy mortgaged property when necessary to secure debts, and to purchase and hold property necessary to carry on its business, but being expressly prohibited from exercising banking powers, cannot loan money on the discount of notes; and this would be so without such express prohibition. *New York Firemen Ins. Co. v. Ely*, 5 Conn. 560. A society incorporated for religious worship has no power to contract for a steamboat excursion, to raise money for church purposes, and cannot recover for expenses or loss of anticipated profits by reason of the defendant's breach of such a contract. *Harriman v. Baptist Church*, 63 Ga. 186.

⁶⁴ *Morville v. Society*, 123 Mass. 129, 136. And see *Union Bank v. Jacobs*, 6 Humph. (Tenn.) 515, 1 Cumming, Cas. Priv. Corp. 302, W. D. Smith, Cas. Corp. 139, Shep. Cas. Corp. 126; *London & N. W. Ry. Co. v. Price*, 11 Q. B. Div. 485, 2 Cumming, Cas. Priv. Corp. 83; *Simpson v. Hotel Co.*, 8 H. L. Cas. 712; *Ft. Worth City Co. v. Smith Bridge Co.*, 151 U. S. 294, 14 Sup. Ct. 839, Shep. Cas. Corp. 98.

⁶⁵ *Munn v. Commission Co.*, 15 Johns. (N. Y.) 52.

its charter, and not immediately needed for its own business;⁶⁶ or to sell property that will no longer be needed at all;⁶⁷ or to borrow money when necessary, and to execute instruments to secure the loan.⁶⁸ A corporation established "for the purpose of manufacturing and selling glass" may contract to purchase glassware from a like corporation to keep up its own stock and supply its customers while its works are being put in order.⁶⁹ A corporation authorized to purchase and hold waterpower created by the erection of dams, and to hold real estate, may, when the water power has been lawfully extinguished, sell its lands, and, as part of the contract of sale, agree to raise the grade.⁷⁰ So, a railroad corporation may agree to transport as a common carrier, over connecting railroads, goods intrusted to it for carriage over its own line.⁷¹ Many other illustrations will appear in the following paragraphs.

As a general rule, subject to exceptions which we shall presently notice, when a corporation is given general authority to engage in business, and there are no special restraints in its charter, it takes the power as a natural person enjoys it, with all its incidents and accessories. It may, like a natural person, make all contracts, not prohibited, which are necessary or proper to enable it to attain its legitimate objects.⁷² A business corporation may incur liability for a reward by offering the same for the apprehension of criminals who have committed crimes against its property or its employés.⁷³ If

⁶⁶ Post, p. 142.

⁶⁷ *Dupee v. Water-Power Co.*, 114 Mass. 37; post, p. 142.

⁶⁸ Post, pp. 145-148.

⁶⁹ *Lyndeborough Glass Co. v. Massachusetts Glass Co.*, 111 Mass. 315. But a corporation for the purpose of manufacturing and selling gold and silver ware cannot, as a part of its business, engage in the purchase and sale of goods of the same general character, but which it cannot advantageously manufacture. *People v. Campbell*, 144 N. Y. 166, 38 N. E. 990.

⁷⁰ *Dupee v. Water-Power Co.*, 114 Mass. 37.

⁷¹ *Swift v. Steamship Co.*, 106 N. Y. 206, 12 N. E. 583, 2 Cumming, Cas. Priv. Corp. 98; *Hill Manuf'g Co. v. Boston & L. R. Corp.*, 104 Mass. 122; *Ohio & M. Ry. Co. v. McCarthy*, 96 U. S. 258.

⁷² *Wright v. Hughes*, 119 Ind. 324, 21 N. E. 907.

⁷³ *Norwood & B. Co. v. Andrews*, 71 Miss. 641, 16 South. 262; *Central R. & B. Co. v. Cheatham*, 85 Ala. 292, 4 South. 828; *American Exp. Co. v. Patterson*, 73 Ind. 430; *Ricord v. Railroad Co.*, 15 Nev. 167.

the charter of a street-railroad company specifies a particular motive power, it excludes all other motive powers; but, if the motive power is in no way limited or defined, any motive power may be used that may be fit and appropriate to enable the company to operate its road.⁷⁴

Power to Purchase Real or Personal Property.

We have already seen that a corporation, unless prohibited, has the capacity to take and hold the title to both real and personal property. It must not be supposed, however, that it has an unlimited power to purchase property, for it has not. It has the implied power, in the absence of express restrictions, to purchase any property, real or personal, that may be reasonably necessary or proper to accomplish the purposes for which it was created.⁷⁵ But it has no power to purchase property for a purpose foreign to the objects of its creation.⁷⁶ A corporation established "for the purpose of manufacturing and selling glass" may contract to purchase glassware from a like corporation, in order to keep up its own stock and supply its customers while its works are being put in order, for this is necessary in order to carry on its business.⁷⁷ A railroad company has the implied power to purchase iron rails for use in building its road, but a purchase of rails to sell them again on speculation would be ultra vires; and the

⁷⁴ *Halsey v. Railway Co.*, 47 N. J. Eq. 380, 20 Atl. 859.

⁷⁵ Personal property: *Lyndeborough Glass Co. v. Massachusetts Glass Co.*, 111 Mass. 815; *Moss v. Averell*, 10 N. Y. 449. Real property: Ante, p. 128; *Co. Litt.* 44c, 300b; 2 Kent, Comm. 281; *Spear v. Crawford*, 14 Wend. (N. Y.) 20; *Nicoll v. Railroad Co.*, 12 N. Y. 121, 1 Cumming, Cas. Priv. Corp. 73; *Old Colony R. Corp. v. Evans*, 6 Gray (Mass.) 25, 38; *Regents of University of Michigan v. Detroit Young Men's Soc.*, 12 Mich. 138. As we have seen, a corporation may purchase and take a fee-simple title to land, though the period of its existence is limited to a term of years. Ante, p. 130.

⁷⁶ Personal property: *Pearce v. Railroad Co.*, 21 How. 441, 1 Cumming, Cas. Priv. Corp. 146; *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148, W. D. Smith, Cas. Corp. 129, *Shep. Cas. Corp.* 75; *Day v. Buggy Co.*, 57 Mich. 146, 23 N. W. 628, 1 Cumming, Cas. Priv. Corp. 261; *Northwestern Packet Co. v. Shaw*, 87 Wis. 655, 1 Cumming, Cas. Priv. Corp. 245; *Bosshardt & Wilson Co. v. Crescent Oil Co.*, 171 Pa. St. 109, 32 Atl. 1120. Real property: *Bank of Michigan v. Niles*, Walk. (Mich.) 99, 1 Cumming, Cas. Priv. Corp. 291; *Case v. Kelly*, 133 U. S. 21, 10 Sup. Ct. 216, 1 Cumming, Cas. Priv. Corp. 100, *Shep. Cas. Corp.* 102.

⁷⁷ *Lyndeborough Glass Co. v. Massachusetts Glass Co.*, 111 Mass. 315.

same is true of other corporations. A manufacturing corporation, though it may purchase materials to use in manufacture, cannot purchase to sell on speculation.⁷⁸ A railroad, steamboat, or canal company can purchase grain or other produce for its own use, but it cannot purchase the same to transport it to another market, and sell it.⁷⁹ A bank authorized by its charter to carry on the business of banking "by discounting bills, notes, and other evidences of debt, * * * and by exercising such incidental powers as may be necessary to carry on such business," has no power to buy notes or bonds, and deal in them in this way.⁸⁰ Nor can a railroad company deal in bills or notes.⁸¹ But either a bank or a railroad company can take bills or notes in the course of its business, as to secure a debt due to it; and the same is true of all other corporations.⁸²

And so it is with purchases of real estate. A railroad, banking, or manufacturing corporation may purchase such real estate as may be necessary for the convenient transaction of its business; but it cannot enter into a valid contract to purchase land, not for use in its business, but as a speculation.⁸³

It has been said that a corporation has no power, unless it is expressly conferred, to purchase property of any kind on credit, unless it is needed for immediate use, or the investment of existing funds.⁸⁴

⁷⁸ *Day v. Buggy Co.*, 57 Mich. 146, 23 N. W. 628, 1 Cumming, Cas. Priv. Corp. 261. And see *Chewacla Lime-Works v. Dismukes*, 87 Ala. 344, 6 South. 122; *Bosshardt & W. Co. v. Crescent Oil Co.*, 171 Pa. St. 109, 32 Atl. 1120.

⁷⁹ *Northwestern Packet Co. v. Shaw*, 37 Wis. 655, 1 Cumming, Cas. Priv. Corp. 245.

⁸⁰ *Farmers' & Mechanics' Bank v. Baldwin*, 23 Minn. 198; *Niagara County Bank v. Baker*, 15 Ohio St. 68; *Talmage v. Pell*, 7 N. Y. 328; *First Nat. Bank v. Pierson*, 24 Minn. 140. But see *National Pemberton Bank v. Porter*, 125 Mass. 333.

⁸¹ *Goodrich v. Reynolds*, 31 Ill. 490.

⁸² *Goodrich v. Reynolds*, supra; *McIntire v. Preston*, 5 Gilm. (Ill.) 48.

⁸³ *President, etc., of Bank of Michigan v. Niles*, Walk. (Mich.) 99, 1 Doug. 401, 1 Cumming, Cas. Priv. Corp. 291; *Case v. Kelly*, 133 U. S. 21, 10 Sup. Ct. 216, 1 Cumming, Cas. Priv. Corp. 106, *Shep. Cas. Corp.* 102; *Pacific R. Co. v. Seely*, 45 Mo. 212.

⁸⁴ *Franklin Co. v. Lewiston Inst. for Savings*, 68 Me. 43, 1 Cumming, Cas. Priv. Corp. 348.

Power to Sell, Lease, Mortgage, or Pledge Property.

In the absence of express restrictions in its charter, and subject to exceptions to be presently noticed, a corporation has the implied power to sell and convey or transfer, or to lease, all or a part of its real or personal property.⁸⁵ And whenever a corporation has the power to borrow money, or to otherwise incur debts, it has, as incidental thereto, unless expressly restricted, the implied power to execute a mortgage on its property, real or personal, or to pledge its property, to secure its debts, whether the debts have been previously contracted, or are contracted at the time, or are to be contracted in the future.⁸⁶ The power of a corporation to execute a mortgage on

⁸⁵ *Brown v. Winnisimmet Co.*, 11 Allen (Mass.) 326; *Hendee v. Pinkerton*, 14 Allen (Mass.) 381, 1 Cumming, Cas. Priv. Corp. 336; *State v. Western Irr. Canal Co.*, 40 Kan. 96, 19 Pac. 349; *Leggett v. Banking Co.*, 1 N. J. Eq. 541; *Dupee v. Water-Power Co.*, 114 Mass. 37; *Aurora A. & H. Soc. v. Paddock*, 80 Ill. 263; *Benbow v. Cook*, 115 N. C. 324, 20 S. E. 453; *Reynolds' Widow v. Commissioners*, 5 Ohio, 204; *Miners' Ditch Co. v. Zellerbach*, 37 Cal. 543; *Simpson v. Hotel Co.*, 8 H. L. Cas. 712. "All civil corporations, * * * unless expressly restrained by the act which establishes them, or by some subsequent act, have, and always have had, an unlimited control over their respective properties, and may alienate in fee, or make what estates they please, for years, for life, or in tail, as fully as any individual may do with respect to his own property." 1 Kyd, Corp. 108.

⁸⁶ *Barry v. Exchange Co.*, 1 Sandf. Ch. (N. Y.) 280; *Curtis v. Leavitt*, 15 N. Y. 9; *Wright v. Hughes*, 119 Ind. 324, 21 N. E. 907; *Eureka Iron & Steel Works v. Bresnahan*, 60 Mich. 332, 27 N. W. 524; *In re Patent File Co.*, 6 Ch. App. 83, 1 Cumming, Cas. Priv. Corp. 322; *W. D. Smith, Cas. Corp.* 125, *Shep. Cas. Corp.* 109; *Aurora A. & H. Soc. v. Paddock*, 80 Ill. 263; *Reichwald v. Hotel Co.*, 106 Ill. 439; *Jones v. Indemnity Co.*, 101 U. S. 622, 1 Cumming, Cas. Priv. Corp. 326; *Railroad Co. v. Howard*, 7 Wall. 392; *Booth v. Robinson*, 55 Md. 419; *Hendee v. Pinkerton*, 14 Allen (Mass.) 381, 1 Cumming, Cas. Priv. Corp. 336; *Thompson v. Lambert*, 44 Iowa, 239; *Detroit v. Mutual Gaslight Co.*, 43 Mich. 594, 5 N. W. 1039; *Evans v. Heating Co.*, 157 Mass. 37, 31 N. E. 698; *Leggett v. Banking Co.*, 1 N. J. Eq. 541; *Gordon v. Preston*, 1 Watts (Pa.) 385; *Leo v. Railway Co.*, 17 Fed. 273; *Duncomb v. Railroad Co.*, 84 N. Y. 190; *Jackson v. Brown*, 5 Wend. (N. Y.) 590; *Memphis & L. R. Co. v. Dow*, 19 Fed. 388; *Bardstown & L. R. Co. v. Metcalfe*, 4 Metc. (Ky.) 199; *Jessup v. Bridge*, 11 Iowa, 572; *Hays v. Coal Co.*, 29 Ohio St. 330. And a corporation having the power to execute a mortgage on its property to secure its debts may, in the absence of special restrictions, execute a mortgage to secure future advances. *Barry v. Exchange Co.*, supra. *Jones v. Indemnity Co.*, supra; *Richards v. Railroad Co.*, 44 N. H. 127.

its property can only be co-extensive with its power to alienate absolutely, since every mortgage may become an absolute conveyance by foreclosure.⁸⁷ In like manner a corporation may make an assignment of its property for the payment of its debts.⁸⁸

In the absence of statutory authority a corporation can neither sell nor mortgage its franchises.⁸⁹ But the power to mortgage corporate franchises may be, and often is, conferred by statute.⁹⁰

By the weight of authority, a railroad company, or other corporation that is vested with the power of eminent domain, and charged with peculiar duties to the public, as telegraph, gas, and water companies, cannot, in the absence of express authority from the legislature, alienate, by absolute conveyance or by lease, property that is essential to enable it to properly perform its functions.⁹¹ Nor, by

⁸⁷ *Com. v. Smith*, 10 Allen (Mass.) 448, 1 Cumming, Cas. Priv. Corp. 331, W. D. Smith, Cas. Corp. 127, Shep. Cas. Corp. 111.

⁸⁸ *Post*, p. 553.

⁸⁹ *Carpenter v. Mining Co.*, 65 N. Y. 43, 50; *Beebe v. Power Co.*, 13 Misc. Rep. 737, 35 N. Y. Supp. 1; *Susquehanna Canal Co. v. Bonham*, 9 Watts & S. (Pa.) 27; *Arthur v. Bank*, 9 Smedes & M. (Miss.) 394; *City Water Co. v. State*, 88 Tex. 600, 32 S. W. 1033; *New Orleans, J. & G. N. R. Co. v. Harris*, 27 Miss. 517; *Stewart v. Jones*, 40 Mo. 140; *Daniels v. Hart*, 118 Mass. 543; *Richardson v. Sibley*, 11 Allen (Mass.) 65.

⁹⁰ See *Lord v. Gas Co.*, 99 N. Y. 547, 2 N. E. 909; *Davidson v. Gaslight Co.*, 99 N. Y. 558, 2 N. E. 892; *East Boston Freight R. Co. v. Eastern R. Co.*, 13 Allen (Mass.) 422.

⁹¹ *Com. v. Smith*, *supra*. "In the case of a railroad company," it was said by Hoar, J., in this case, "created for the express and sole purpose of constructing, owning, and managing a railroad; authorized to take land for this purpose under the power of eminent domain; whose powers are to be exercised by officers expressly designated by statute; having public duties, the discharge of which is the leading object of its creation; required to make returns to the legislature,—there are certainly great, and, in our opinion, insuperable objections to the doctrine that its franchise can be alienated, and its powers and privileges conferred by its own act upon another person or body, without authority other than that derived from the fact of its own incorporation. The franchise to be a corporation clearly cannot be transferred by any corporate body, of its own will. Such a franchise is not in its own nature transmissible. * * * And although the franchise to exist as a corporation is distinguishable from the franchises to be enjoyed and used by the corporation after its creation, yet the transfer of the latter differs essentially from the mere alienation of ordinary corporate property. The right of a railroad company to continue in business depends upon the performance of its public duties. Having once established its road, if

the weight of authority, can it execute a mortgage on such property, in the absence of express authority, even to secure legitimate debts; for, as has been stated, the power to mortgage can only be co-extensive with the power to alienate absolutely, since every mortgage may become an absolute conveyance by foreclosure.⁹² A railroad company, or similar corporation, however, has the same implied power as any other corporation, in the absence of special restraint, to alienate property which it has acquired otherwise than by the exercise of the power of eminent domain, and which is not necessary to enable it to perform its functions.⁹³ And it has, of course, the same power to mortgage such property, if it does so for an authorized purpose.⁹⁴

The legislature generally expressly authorizes these quasi public corporations to mortgage their property and franchises under certain circumstances. Of course, authority to mortgage for a specified purpose would, under familiar rules of construction, exclude all other

that and the franchise of managing, using, and taking tolls and fares upon the same are alienated, its whole power to perform its most important functions is at an end. A manufacturing company may sell its mill, and buy another; but a railroad company cannot make a new railroad at its pleasure." And see *Beman v. Rufford*, 1 Sim. (N. S.) 550; *Winch v. Railway Co.*, 5 De Gex & S. 562; *Thomas v. Railroad Co.*, 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164, W. D. Smith, Cas. Corp. 132, Shep. Cas. Corp. 70; *New York & M. L. R. Co. v. Winans*, 17 How. 30; *Black v. Canal Co.*, 22 N. J. Eq. 390; *Central Transp. Co. v. Pullman's Palace-Car Co.*, 139 U. S. 24, 11 Sup. Ct. 478, 2 Cumming, Cas. Priv. Corp. 44; *St. Louis, V. & T. H. R. Co. v. Terre Haute & I. R. Co.*, 145 U. S. 393, 12 Sup. Ct. 953, 2 Cumming, Cas. Priv. Corp. 78; *American Union Tel. Co. v. Union Pac. Ry. Co.*, 1 McCrary, 188, 1 Fed. 745, 1 Cumming, Cas. Priv. Corp. 284; *Chicago Gaslight & Coke Co. v. People's Gaslight & Coke Co.*, 121 Ill. 530, 13 N. E. 169; *Coe v. Railroad Co.*, 10 Ohio St. 372; note 85, *supra*, and cases there cited. But see *Bardstown & L. R. Co. v. Metcalfe*, 4 Metc. (Ky.) 199; *Miller v. Railroad Co.*, 36 Vt. 452.

⁹² *Com. v. Smith*, *supra*, and other cases cited above; *Richardson v. Sibley*, 11 Allen (Mass.) 65. But see *Hunt v. Gaslight Co.*, 95 Tenn. 186, 31 S. W. 1006, where it was held that, when its charter does not confer the power of eminent domain or exclusive privilege, a gas company can mortgage its entire property to secure bonds and floating indebtedness, though the charter does not expressly confer the right to mortgage.

⁹³ *Hendee v. Pinkerton*, 14 Allen (Mass.) 381, 1 Cumming, Cas. Priv. Corp. 836; *Coe v. Railroad Co.*, 10 Ohio St. 372.

⁹⁴ *Hendee v. Pinkerton*, *supra*.

purposes. If the legislature confers upon such a corporation power to mortgage its property without limitation, it authorizes a mortgage of the entire corporate property.⁹⁵ If it confers the power to sell and transfer or alien absolutely, this will give the power to mortgage.⁹⁶ And power to mortgage includes, as a necessary incident, the power to borrow money and issue bonds therefor.⁹⁷ Where a railroad company has express authority to mortgage its property, a mortgage executed by it, covering both its property and franchise, will not be avoided as to the property by the fact that there was no authority to mortgage the franchise.⁹⁸

Power to Borrow Money.

Except in so far as there may be express restrictions in its charter, a private corporation may, like an individual, borrow money, whenever the nature of its business renders it proper or expedient that it should do so.⁹⁹ But if the purposes for which a corporation is organized and chartered do not require it to borrow money, it cannot do so; and it cannot do so for an unauthorized purpose.¹⁰⁰

⁹⁵ *Pumphrey v. Threadgill*, 9 Tex. Civ. App. 184, 28 S. W. 450. As to what passes under a general railroad mortgage, the effect on after-acquired property, etc. see *Philadelphia, W. & B. R. Co. v. Woelpper*, 64 Pa. St. 366; *Galveston, H. & H. R. Co. v. Cowdrey*, 11 Wall. 459; *Fosdick v. Schall*, 99 U. S. 235; *Hancock v. Trust Co.*, 105 U. S. 77.

⁹⁶ *East Boston Freight R. Co. v. Eastern R. Co.*, 13 Allen (Mass.) 422; *McAllister v. Plant*, 54 Miss. 106.

⁹⁷ *Gloninger v. Railroad Co.*, 139 Pa. St. 13, 21 Atl. 211.

⁹⁸ *Id.*

⁹⁹ *Barry v. Exchange Co.*, 1 Sandf. Ch. (N. Y.) 280; *Curtis v. Leavitt*, 15 N. Y. 9; *Nelson v. Eaton*, 26 N. Y. 410; *Wright v. Hughes*, 119 Ind. 324, 21 N. E. 907; *In re Patent File Co.*, 6 Ch. App. 83, 1 Cumming, Cas. Priv. Corp. 322, W. D. Smith, Cas. Corp. 125, Shep. Cas. Corp. 109; *Heironimus v. Sweeney* (Md.) 34 Atl. 823; *Reichwald v. Hotel Co.*, 106 Ill. 439; *Fifth Ward Sav. Bank v. First Nat. Bank*, 48 N. J. Law, 513, 7 Atl. 318; *Booth v. Robinson*, 55 Md. 419; *Commercial Bank of New Orleans v. Newport Manuf'g Co.*, 1 B. Mon. (Ky.) 13; *Union Gold Min. Co. v. Rocky Mountain Nat. Bank*, 2 Colo. 248; *Bradbury v. Canoe Club*, 153 Mass. 77, 26 N. E. 132; *Hays v. Coal Co.*, 29 Ohio St. 330. A mutual fire insurance company can borrow money to pay losses, and give its notes therefor. *Orr v. Insurance Co.*, 114 Pa. St. 387, 6 Atl. 696.

¹⁰⁰ *In re Cork & Youghal Ry. Co.*, 4 Ch. App. 748, 1 Cumming, Cas. Priv. Corp. 265; *In re National Building Society*, 5 Ch. App. 309, 1 Cumming, Cas. Priv. Corp. 274; *Wenlock v. River Dee Co.*, 19 Q. B. Div. 155, 1 Cumming,

It has been held, for instance, that building associations have no implied power to borrow money.¹⁰¹ It seems clear that they have no power to borrow money for the purpose of lending it out again, for this is not within their purpose.¹⁰²

Power to Execute Bonds.

Corporations, including railroad companies, have the implied power to execute a bond for any purpose for which they may lawfully contract a debt, in the absence of restrictions in their charter. "A bond is merely an obligation under seal. A corporation having the capacity to sue and be sued, the right to make contracts, under which they may incur debts, and the right to make and use a common seal, a contract under seal is not only within the scope of its powers, but was originally the usual, and peculiarly appropriate, form of corporate agreement."¹⁰³ When a statute specifies a particular manner in which bonds shall be executed by a corporation, as is often the case, a failure to comply with the statute renders the bonds invalid.¹⁰⁴

Bonds of corporations, and the coupons attached thereto, will be regarded as negotiable instruments, and as subject to the rules of law relating to such instruments, if it appears from the form in which they were issued, and the mode of giving them circulation, that they were intended to have this character; and they will be transferable like negotiable bills and notes, and subject to the rules protecting bona fide holders.¹⁰⁵

Cas. Priv. Corp. 277; Bacon v. Insurance Co., 31 Miss. 116; Adams & Westlake Co. v. Deyette (S. D.) 65 N. W. 471.

¹⁰¹ In re National Building Society, *supra*.

¹⁰² State v. Oberlin Building & Loan Ass'n, 35 Ohio St. 258, 1 Cumming, Cas. Priv. Corp. 566.

¹⁰³ Com. v. Smith, 10 Allen (Mass.) 448, 1 Cumming, Cas. Priv. Corp., 331, W. D. Smith, Cas. Corp. 127, Shep. Cas. Corp. 111. And see White Water Valley Canal Co. v. Vallette, 21 How. 414; Barry v. Exchange Co., 1 Sandf. Ch. (N. Y.) 280; Curtis v. Leavitt, 15 N. Y. 9.

¹⁰⁴ Com. v. Smith, *supra*.

¹⁰⁵ White v. Railroad Co., 21 How. 575, 1 Cumming, Cas. Priv. Corp. 133; American Nat. Bank v. American Wood-Paper Co., Index QQ, 139, 32 Atl. 305; Galveston, H. & H. R. Co. v. Cowdrey, 11 Wall. 459; Carr v. Le Fevre, 27 Pa. St. 413; City of Lexington v. Butler, 14 Wall. 282; Philadelphia & R. R. Co. v. Smith, 105 Pa. St. 195; Philadelphia & R. R. Co. v. Fidelity Insurance,

Power to Make Negotiable Instruments.

It has been held in England that a corporation cannot accept a bill of exchange unless expressly empowered to do so.¹⁰⁶ The decision is based on the peculiar character of such an instrument, and on the fact that, as it excludes, as against a bona fide holder for value, any inquiry into the consideration, it would prevent the defense of ultra vires. This reasoning applies also to the making of negotiable promissory notes, and the indorsing of bills and notes. In this country the rule is different. A corporation has the implied power to make or indorse promissory notes, and to draw, indorse, or accept bills of exchange, if it is a usual or appropriate means of accomplishing the objects and purposes for which it was created. It has the power to execute negotiable instruments when it has the power to borrow money.¹⁰⁷ But if such acts are foreign to the purposes of the charter, or repugnant thereto, the power does not exist.¹⁰⁸ The right to set up the defense that the execu-

Trust & Safe-Deposit Co., Id. 216; *Curtis v. Leavitt*, 15 N. Y. 9; *Woodbury v. Railroad Co.*, 72 Fed. 371.

¹⁰⁶ *Bateman v. Railway Co.*, L. R. 1 C. P. 499, 1 Cumming, Cas. Priv. Corp. 312.

¹⁰⁷ *Union Bank v. Jacobs*, 6 Humph. (Tenn.) 515, 1 Cumming, Cas. Priv. Corp. 302, W. D. Smith, Cas. Corp. 139, Shep. Cas. Corp. 126; *Fifth Ward Sav. Bank v. First Nat. Bank*, 48 N. J. Law, 513, 7 Atl. 318; *Moss v. Averell*, 10 N. Y. 449; *Mott v. Hicks*, 1 Cow. (N. Y.) 513; *Munn v. Commission Co.*, 15 Johns. (N. Y.) 44; *Olcott v. Railroad Co.*, 27 N. Y. 546; *Commercial Bank v. Newport Manuf'g Co.*, 1 B. Mon. (Ky.) 13; *Richmond, F. & P. R. Co. v. Snead*, 19 Grat. (Va.) 354; *Goodrich v. Reynolds*, 31 Ill. 490; *Ward v. Johnson*, 95 Ill. 215; *McIntire v. Preston*, 5 Gilman (Ill.) 48; *Orr v. Insurance Co.*, 114 Pa. St. 387, 6 Atl. 696; *Hardy v. Merriweather*, 14 Ind. 203; *Ex parte Estabrook*, 2 Low. 547, Fed. Cas. No. 4,534; *Bradbury v. Canoe Club*, 153 Mass. 77, 26 N. E. 132; *Narragansett Bank v. Atlantic Silk Co.*, 3 Metc. (Mass.) 282. A railroad company, for instance, being empowered to construct and operate its road, may incur debts in carrying out its object; and, where a debt has been lawfully incurred, it may execute a promissory note or accept a bill of exchange in payment thereof, or it may raise money on a bill or note for the purpose of making such payment. *Union Bank v. Jacobs*, supra.

¹⁰⁸ *National Park Bank v. German-American M. W. & S. Co.*, 116 N. Y. 281, 22 N. E. 567, 1 Cumming, Cas. Priv. Corp. 318, Shep. Cas. Corp. 132; *Bacon v. Insurance Co.*, 31 Miss. 116. Thus, a corporation cannot, even for a consideration paid, bind itself by indorsing promissory notes for accommodation of the

tion or indorsement of a negotiable instrument by a corporation was ultra vires, in order to defeat a recovery by a bona fide holder for value, will be shown in explaining the effect of ultra vires contracts.¹⁰⁹

Contracts of Suretyship and Guaranty—Accommodation Paper.

As a general rule, to authorize a corporation to become guarantor or surety for another person or corporation, even for a valuable consideration paid to it, there must be an express grant of such power in its charter, or it must have been chartered for the purpose of becoming surety for others. The power is not incident to corporations for railroading, banking, insurance, manufacturing, etc.¹¹⁰ Nor has a corporation any implied authority or power to accept a bill of exchange as an accommodation, or to execute an accommodation note, or to indorse a bill or note as an accommodation.¹¹¹ Such contracts as these are clearly foreign to the objects

maker. *National Park Bank v. German-American M. W. & S. Co.*, supra. And see note 111, infra, and cases there cited.

¹⁰⁹ Post, p. 175.

¹¹⁰ *National Park Bank v. German-American M. W. & S. Co.*, 116 N. Y. 281, 22 N. E. 567, 1 Cumming, Cas. Priv. Corp. 318, Shep. Cas. Corp. 132; *Memphis Grain & Elevator Co. v. Memphis & O. R. Co.* (Tenn.) 5 S. W. 52; *Madison, Watertown & Milwaukee Plank-Road Co. v. Watertown & Portland Plank-Road Co.*, 7 Wis. 59; *Lucas v. Transfer Co.*, 70 Iowa, 542; 30 N. W. 771; *Culver v. Real-Estate Co.*, 91 Pa. St. 367; *Hall v. Turnpike Co.*, 27 Cal. 255; *Filon v. Brewing Co.*, 60 Hun, 582, 15 N. Y. Supp. 57; *Humboldt Min. Co. v. American Manufacturing, Mining & Milling Co.*, 10 C. C. A. 415, 62 Fed. 358; *Aetna Nat. Bank v. Charter Oak Life Ins. Co.*, 50 Conn. 167. No authority in a corporation to lend its credit to another is to be implied from the fact that it may be beneficial to the corporation to do so. *Germania Safety-Vault & Trust Co. v. Boynton*, 19 C. C. A. 118, 71 Fed. 797. "It is no part of the ordinary business of commercial corporations, and, a fortiori, still less so of noncommercial corporations, to become surety for others. Under ordinary circumstances, without positive authority in this behalf in the grant of corporate power, all engagements of this description are ultra vires, whether in the indirect form of going on accommodation bills, or otherwise becoming liable for the debts of others." *Green's Brice, Ultra Vires*, 252.

¹¹¹ *National Park Bank v. German-American M. W. & S. Co.*, supra; *National Bank v. Young*, 41 N. J. Eq. 531, 7 Atl. 488; *Ex parte Estabrook*, 2 Low. 547, Fed. Cas. No. 4,534; *Aetna Nat. Bank v. Charter Oak Life Ins. Co.*, 50 Conn. 167. See *National Bank v. John G. Mattingly & Sons* (Ky.) 33 S. W. 415, where recovery was allowed on accommodation paper under peculiar circumstances.

of most corporations. The fact that a consideration is received by the corporation for entering into the contract can make no difference.¹¹² We shall see, in another place that a corporation cannot always successfully defend against accommodation paper, where it has passed into the hands of a bona fide purchaser for value;¹¹³ but this is based on peculiar reasons, and is not inconsistent with want of power to make the contract.

There may be circumstances under which a corporation would have the power to guaranty the debt of another person or corporation. Being authorized to make all contracts that may be necessary for accomplishing the purpose of its creation, a corporation, in making a contract which it is authorized to make, may, as a part of the consideration, become a guarantor. Thus, a railroad company, for the purpose of disposing of bonds issued to it by a municipal corporation in payment of subscriptions to its stock, may guaranty their payment.¹¹⁴ So, where one railroad company makes an authorized lease of its road to another, the lessee may, as part of the consideration for the contract, guaranty the payment of bonds issued by the lessor.¹¹⁵ And a railroad company, which has power by its charter to issue its own bonds, has power to guaranty the bonds of another railroad company, which it has taken in payment of a debt due it, and which it sells or transfers in payment of its own debt; the guaranty being given to enable it to dispose of the bonds to better advantage.¹¹⁶ And corporations hold-

¹¹² *National Park Bank v. German-American M. W. & S. Co.*, *supra*.

¹¹³ *Post*, p. 175.

¹¹⁴ *Chicago, R. I. & P. R. Co. v. Howard*, 7 Wall. 392.

¹¹⁵ *Low v. Railroad Co.*, 52 Cal. 53. In *Wheeler, Osgood & Co. v. Everett Land Co.* (Wash.) 45 Pac. 316, it was held that, where it appears that it was customary for corporations dealing in lumber to become sureties on building contractors' bonds in order to get business, articles of incorporation providing that the corporation may do all things necessary to carry on the business of manufacturing and dealing in lumber will be construed as granting the power to become surety on contractors' bonds, in the absence of express prohibition. This is contrary to the cases cited in note 110, *supra*, and cannot be sustained on authority.

¹¹⁶ *Rogers L. & M. Works v. Southern Railroad Ass'n*, 34 Fed. 278. And see *Arnot v. Railway Co.*, 67 N. Y. 315; *Ellerman v. Stockyards Co.*, 49 N. J. Eq. 217, 23 Atl. 287; *Marbury v. Land Co.*, 10 C. C. A. 393, 62 Fed. 335.

ing negotiable paper may indorse the same for the purpose of negotiating it.¹¹⁷

Contracts of Partnership.

A corporation has no power to enter into a contract of partnership, unless the power is expressly conferred upon it. The power will not be implied, for the manner in which the business of a corporation is conducted is inconsistent with such a contract.¹¹⁸ As was said in a Massachusetts case, in reference to a manufacturing corporation which had undertaken to form a partnership: "There is one obvious and important distinction between such a society as this charter creates and that of a partnership. An act of the corporation, done either by direct vote or by agents authorized for the purpose, is the manifestation of the collected will of the society. No member of the corporation, as such, can bind the society. In a partnership, each member binds the society as a principal. If, then, this corporation can enter into partnership with an individual, there would be two principals, the legal person and the natural person, each having, within the scope of the society's business, full authority to manage its concerns, including even the disposition of its property."¹¹⁹ An agreement among a number of corporations, or between corporations and natural persons, engaged in manufacture, to select a committee composed of representatives from each, and to turn over to such committee the prop-

¹¹⁷ *Bank of Genesee v. Patchin Bank*, 13 N. Y. 309.

¹¹⁸ *Whittenton Mills v. Upton*, 10 Gray (Mass.) 582, 1 Cumming, Cas. Priv. Corp. 399; *Mallory v. Oil Works*, 86 Tenn. 598, 8 S. W. 396; *Central R. & B. Co. v. Smith*, 76 Ala. 572; *Marine Bank v. Ogden*, 29 Ill. 248. Cf. *Catskill Bank v. Gray*, 14 Barb. (N. Y.) 471, 2 Cumming, Cas. Priv. Corp. 88, where a corporation was held liable to third persons as a partner. And see *Allen v. Woonsocket Co.*, 11 R. I. 288, 2 Cumming, Cas. Priv. Corp. 91. If a corporation does enter into and carry out a contract of partnership, and receives more than its share of the profits, it has been held that it cannot defeat an action by the other party to recover his share on the plea of ultra vires. *Standard Oil Co. v. Scofield*, 16 Abb. N. C. 372, 2 Cumming, Cas. Priv. Corp. 95.

¹¹⁹ *Whittenton Mills v. Upton*, supra. But it has been held that it is not ultra vires for a corporation to enter into a contract with an individual to engage in a certain venture, and share profits and losses, where all the management of the enterprise is intrusted to the corporation. *Bates v. Coronado Beach Co.*, 109 Cal. 160, 41 Pac. 855.

erty and machinery of each, to be managed and operated by the committee for the common benefit, the profits and losses to be shared in equal proportions, and the arrangement to last for a specified time, is a contract of partnership, and therefore within this rule.¹²⁰

The rule that corporations cannot enter into a partnership agreement does not prevent a corporation and a natural person, or two corporations, from entering into a joint contract, or taking property as tenants in common. Thus, two corporations, or a corporation and a natural person, may be mortgagees in the same mortgage, or obligees in the same bond, or promisees in the same note, and, in like manner, they may execute a joint note, bond, or other contract. So, where money is deposited in bank in the joint names of two corporations, they are tenants in common or joint creditors, and may maintain a joint action to enforce their rights.¹²¹

Power to Acquire and Hold Stock in Another Corporation.

Though it is otherwise in England and in some of our states,¹²² it is very generally held in this country that a corporation has no implied power to subscribe for, purchase, or hold stock in another corporation.¹²³ Not only is it without the power to hold the stock as its own absolutely, but it has been held that it has no power to hold it in pledge, if it appears as owner on the books of the cor-

¹²⁰ Mallory v. Oil Works, *supra*.

¹²¹ New York & S. Canal Co. v. Fulton Bank, 7 Wend. (N. Y.) 412, 2 Cumming, Cas. Priv. Corp. 87; Marine Bank v. Ogden, 29 Ill. 248.

¹²² In re Asiatic Banking Corp., L. R. 4 Ch. App. 252, 1 Cumming, Cas. Priv. Corp. 359, W. D. Smith, Cas. Corp. 21, Shep. Cas. Corp. 113; In re Barned's Banking Co., L. R. 3 Ch. App. 105; Iowa Lumber Co. v. Foster, 49 Iowa, 25; Calumet Paper Co. v. Stotts Inv. Co. (Iowa) 64 N. W. 782.

¹²³ Franklin Co. v. Lewiston Inst. for Savings, 68 Me. 43, 1 Cumming, Cas. Priv. Corp. 343; Franklin Bank v. Commercial Bank, 36 Ohio St. 350; 1 Cumming, Cas. Priv. Corp. 348, W. D. Smith, Cas. Corp. 26; Talmage v. Pell, 7 N. Y. 328; Nassau Bank v. Jones, 95 N. Y. 115, 1 Cumming, Cas. Priv. Corp. 293; Pearson v. Concord R. Corp., 62 N. H. 537; Mechanics' & Workingmen's Mut. Sav. Bank v. Meriden Ag. Co., 24 Conn. 159; Milbank v. Railroad Co., 64 How. Prac. (N. Y.) 20, 1 Cumming, Cas. Priv. Corp. 353; Byrne v. Manufacturing Co., 65 Conn. 336, 31 Atl. 833; Sumner v. Marcy, 3 Woodb. & M. 105, Fed. Cas. No. 13,609; Denny Hotel Co. v. Schram, 6 Wash. 134, 32 Pac. 1002; Hazlehurst v. Railroad Co., 43 Ga. 13; Buckeye Marble & Freestone Co. v. Harvey, 92 Tenn. 115, 20 S. W. 427; Valley Ry. Co. v. Lake Erie Iron Co., 46 Ohio, 44, 18 N. E. 486; Knowles v. Sandercock,

poration.¹²⁴ "Were this not so," it has been said, "one corporation, by buying up the majority of the shares of the stock of another, could take the entire management of its business, however foreign such business might be to that which the corporation so purchasing said shares was created to carry on. A banking corporation could become the operator of a railroad, or carry on the business of manufacturing, and any other corporation could engage in banking by obtaining the control of the bank's stock. Nor would this result follow any the less certainly if the shares of stock were received in pledge only, to secure the payment of a debt, provided the shares were transferred on the books of the company to the name of the pledgee. A person in whose name the stock of the corporation stands on the books of the corporation is, as to the corporation, a stockholder, and has the right to vote upon the stock."¹²⁵

It is well settled, however, that a corporation may in good faith take and hold stock in another corporation to secure a loan previously made by it, or a debt which is due to it, or in payment of such loan or debt.¹²⁶

Though dealing in stocks by a national bank is not expressly prohibited by the national banking act, such a prohibition is implied from a failure to grant the power.¹²⁷ A national bank, however, in the honest exercise of the power to compromise a doubtful debt owing to it, or one owing by it, may take stocks with a view to

107 Cal. 629, 40 Pac. 1047. A corporation cannot organize a subordinate corporation. *Lagrove v. Timmerman* (S. C.) 24 S. E. 290. Contra, by statute. The statute ratifies prior acquisition of stock. *In re Buffalo, N. Y. & E. R. Co.* (Sup.) 37 N. Y. Supp. 1048. A foreign corporation cannot be allowed to purchase the stock of, and so control, a domestic corporation. *Buckeye Marble & Freestone Co. v. Harvey*, supra. A corporation may in some states be formed for the purpose of dealing in stocks, bonds, etc., in which case it may purchase and hold stock. *Market St. Ry. Co. v. Hellman*, 109 Cal. 571, 42 Pac. 225.

¹²⁴ *Franklin Bank v. Commercial Bank*, 36 Ohio St. 350, 1 Cumming, Cas. Priv. Corp. 348, W. D. Smith, Cas. Corp. 26.

¹²⁵ *Id.*

¹²⁶ *Talmage v. Pell*, 7 N. Y. 328; *First Nat. Bank v. National Exch. Bank*, 92 U. S. 122, 1 Cumming, Cas. Priv. Corp. 368.

¹²⁷ *First Nat. Bank v. National Exch. Bank*, 92 U. S. 122, 1 Cumming, Cas. Priv. Corp. 368.

their subsequent sale or conversion into money, so as to make good or reduce an anticipated loss. This is not a dealing in stocks.¹²⁸

It was held in a late New York case that a purely private corporation, performing no quasi public duties, could, with the consent of its stockholders, sell all its property to another corporation, and take stock of the latter company in payment therefor.¹²⁹

Power of Corporation to Acquire and Hold Its Own Stock.

In England and in most of our states it is held that, unless expressly authorized, a corporation has no power to purchase its own stock, either for the purpose of selling or reissuing it, or for the purpose of holding or retiring it, as such a transaction is considered foreign to the purposes of a corporation, and an illegitimate employment of its capital.¹³⁰ This doctrine has also been sustained on the ground that to allow a corporation to buy in its own stock, and thereby release shareholders, would be inconsistent with the individual liability imposed by statute upon shareholders for the debts of the corporation.¹³¹ "I can quite understand," said Lord Herschell, "that the directors of a company may sometimes desire that the shareholders should not be numerous, and that they should be persons likely to leave them with a free hand to carry on their operations. But I think it would be most dangerous to countenance the view that, for reasons such as these, they could legitimately expend the moneys of the company to any extent they please in the purchase of its shares. No doubt, if certain shareholders are disposed to hamper the proceedings of the company, and are willing to sell their

¹²⁸ Id.

¹²⁹ *Holmes & Griggs Manuf'g Co. v. Holmes & W. Metal Co.*, 127 N. Y. 252, 27 N. E. 831, 2 Cumming, Cas. Priv. Corp. 85. And see *Treadwell v. Manufacturing Co.*, 7 Gray (Mass.) 393. But see *McCutcheon v. Merz Capsule Co.*, 71 Fed. 787, 19 C. C. A. 108.

¹³⁰ *Trevor v. Whitworth*, L. R. 12 App. Cas. 409, 1 Cumming, Cas. Priv. Corp. 384; *Coppin v. Railroad Co.*, 38 Ohio St. 275, 1 Cumming, Cas. Priv. Corp. 393, W. D. Smith, Cas. Corp. 29, Shep. Cas. Corp. 121; *State v. Oberlin Bldg. & Loan Ass'n*, 35 Ohio St. 258, 1 Cumming, Cas. Priv. Corp. 566. And see *Adams & Westlake Co. v. Deyette* (S. D.) 65 N. W. 471; *Price v. Coal Co.* (Ky.) 32 S. W. 267. A sale of its stock by a corporation, with an option to the purchaser to return it, and receive back his money, is not void as a contract by the corporation to purchase its own stock. *Vent v. Spice Co.* (Minn.) 67 N. W. 70.

¹³¹ *Coppin v. Railroad Co.*, supra.

shares, they may be bought out; but this must be done by persons, existing shareholders or others, who can be induced to purchase the shares, and not out of the funds of the company."¹³² This doctrine is not inconsistent with the forfeiture or surrender of shares in a corporation, which involve no payment by the company.¹³³

The doctrine does not prevent a corporation from taking its own stock as security for, or in payment of, a debt due to it.¹³⁴ The national banking act expressly prohibits a national bank from making any loan or discount on the security of the shares of its own capital stock, or from becoming the purchaser or holder thereof, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and it is further provided that stock so purchased or acquired shall, within six months from the date of its purchase, be sold or disposed of at public or private sale, or, in default thereof, a receiver may be appointed to close up the business.¹³⁵

The fact that a bank or other corporation has made an ultra vires purchase of its own stock, or has made a loan upon its own stock, and acquired it under the contract, can only be objected to by private individuals before the contract has been executed, or, at least, while the stock is still in the hands of the corporation. The objection cannot be raised after the contract has been fully executed, the security sold, and the proceeds applied to payment of the debt.¹³⁶

In some states the doctrine that a corporation cannot purchase its own stock is not recognized, but, on the contrary, it is held that, in the absence of express restrictions in its charter or in some statute, a corporation has the implied power to acquire and hold its own stock, and to sell, reissue, or retire the same, as it may see

¹³² *Trevor v. Whitworth*, *supra*.

¹³³ *Id.*

¹³⁴ *Taylor v. Exporting Co.*, 6 Ohio, 177; *Coppin v. Railroad Co.*, *supra*; *First Nat. Bank v. National Exch. Bank*, 92 U. S. 122; *Ex parte Holmes*, 5 Cow. (N. Y.) 426; *City Bank v. Bruce*, 17 N. Y. 507; *State v. Smith*, 48 Vt. 266, 284; *Williams v. Manufacturing Co.*, 3 Md. Ch. 418, 452. And it has been held that a corporation may sell property not needed by it, and take its own stock in payment therefor. *Dupee v. Water-Power Co.*, 114 Mass. 37.

¹³⁵ *First Nat. Bank v. Stewart*, 107 U. S. 676, 2 Sup. Ct. 778, 1 Cumming, Cas. Priv. Corp. 397.

¹³⁶ *First Nat. Bank v. Stewart*, *supra*.

fit;¹³⁷ that it can take its own stock, for instance, as collateral security for a loan made by it at the time, or may purchase the same outright.¹³⁸ And in such a case the stock does not merge, but may be reissued.¹³⁹ This power, as recognized in these states, though most frequently exercised by banks, is not limited to such corporations, but extends also to railroad companies, manufacturing companies, and all other kinds of joint-stock corporations.¹⁴⁰

Even in these states, however, it is held that the power cannot be exercised to the prejudice of existing creditors of the corporation. If it is so exercised, a court of equity will grant relief. And even though the corporation may be solvent, and may act in good faith, a purchase of its own shares by it may be impeached by existing creditors, who are prejudiced thereby. This rule has been put on the ground that the capital stock of a corporation is "a fund set apart for the payment of its debts,"¹⁴¹ and that property paid by a corporation in the purchase of its stock may be followed by an injured creditor into the hands of any one but a bona fide purchaser for value.¹⁴² But it is not necessary to resort to the trust-fund doctrine. Such a transaction is a fraud on existing creditors.¹⁴³ If based on the trust-fund doctrine, the purchase could be impeached by subsequent creditors; and it is well settled that this cannot be done.¹⁴⁴

Presumption.

The presumption of law being in favor of right doing, the contracts of a corporation will be presumed to be within the legitimate scope and purpose of the corporation until the contrary appears, and the burden of showing the contrary rests upon the party who objects.¹⁴⁵ The presumption is that a conveyance to

¹³⁷ *Chicago, P. & S. W. R. Co. v. Town of Marseilles*, 84 Ill. 145, 643, 1 Cumming, Cas. Priv. Corp. 374, 377; *W. D. Smith, Cas. Corp.* 32, *Shep. Cas. Corp.* 118.

¹³⁸ See cases above cited.

¹³⁹ *State v. Smith*, 48 Vt. 266.

¹⁴⁰ *Chicago, P. & S. W. R. Co. v. Town of Marseilles*, supra; *State v. Smith*, supra.

¹⁴¹ *Sanger v. Upton*, 91 U. S. 56, 60.

¹⁴² *Clapp v. Peterson*, 104 Ill. 26, 1 Cumming, Cas. Priv. Corp. 380.

¹⁴³ *Post*, p. 549.

¹⁴⁴ *Post*, p. 550.

¹⁴⁵ *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148, *W.*

a corporation authorized to acquire land for some purposes only was taken by it for a lawful purpose. If the purpose was in fact illegal, the fact must be affirmatively shown.¹⁴⁶

SAME—FORM AND MODE OF CORPORATE CONTRACTS.

58. It was at one time held that, save in a few cases, a corporation could not contract except under its corporate seal. It is now settled, however, that, except in so far as there may be express restrictions in its charter or in some statute, a corporation can contract by resolutions or by agents, and without a seal, in any case where a natural person could contract without a seal. And, like a natural person, it may be liable quasi ex contractu.

59. If the charter of a corporation, or some statute, prescribes a particular mode or form for entering into contracts, that mode and form must be followed. But—

(a) The statute must be mandatory, and not merely directory.

(b) The statute will not be so construed as to prevent recovery, where the contract has been executed and consideration furnished by one of the parties, unless such a legislative intent is clear.

60. A seal need not be affixed by the officers of a corporation. It is sufficient if they direct it to be done by another, or adopt a seal affixed by another.

61. A seal does not prevent inquiry into the consideration for a corporate contract for the purpose of determining whether it is ultra vires.

D. Smith, Cas. Corp. 129, Shep. Cas. Corp. 75; Thomas v. Railroad Co., 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164, W. D. Smith, Cas. Corp. 182, Shep. Cas. Corp. 70; Barker v. Insurance Co., 3 Wend. (N. Y.) 94; Nelson v. Eaton, 26 N. Y. 410; Patterson v. Robinson, 116 N. Y. 193, 22 N. E. 372; Ellerman v. Stock Yards Co., 49 N. J. Eq. 217, 23 Atl. 287.

¹⁴⁶ Chautauqua County Bank v. Risley, 19 N. Y. 369; Regents of University of Michigan v. Detroit Young Men's Society, 12 Mich. 138.

Under the old common law, the general rule was that a corporation could only manifest its intention, and so enter into contracts, by the use of its corporate seal.¹⁴⁷ To this rule there were some exceptions, based upon necessity or convenience. Whenever to hold the general rule applicable would occasion very great inconvenience, or tend to defeat the very object for which the corporation was created, it was allowed to contract without seal. The retainer of an inferior servant,¹⁴⁸ and the doing of acts frequently recurring or too insignificant to be worth the trouble of affixing the common seal, were established exceptions. And companies incorporated for the purpose of trade were allowed to accept bills of exchange and execute promissory notes.¹⁴⁹ At length the exceptions were extended so much that it came to be the established rule that, though a corporation could not contract directly except under its corporate seal, yet it might, by mere vote or other corporate act, not under seal, appoint an agent, whose acts and contracts, within the scope of his authority, would be binding upon the corporation. As soon as this doctrine became established, the old rule requiring the use of the seal began to be more and more disregarded, until now it is no longer recognized to any extent, if at all.¹⁵⁰ On the contrary, unless the charter or some statute provides otherwise, a corporation need only use a seal where an individual would be required to use one. In all cases where it is not so restricted, it may appoint or employ an attorney, agent, or servant by parol or by writing not under seal;¹⁵¹ and any

¹⁴⁷ "A corporation," said Blackstone, "being an invisible body, cannot manifest its intention by any personal act or oral discourse. It therefore speaks and acts only by its common seal. For, though the particular members may express their private consents to any act by words or signing their names, yet this does not bind the corporation; it is the fixing of the seal, and that only, which unites the several assents of the individuals who compose the community, and makes one joint assent of the whole." 1 Bl. Comm. 475. See *Horn v. Ivy*, 1 Vent. 47; *East London Waterworks Co. v. Bailey*, 12 Moore, 532, 4 Bing. 283; *Dunston v. Coke Co.*, 8 Barn. & Adol. 125.

¹⁴⁸ See *Horn v. Ivy*, 1 Vent. 47.

¹⁴⁹ See *Church v. Coke Co.*, 6 Adol. & El. 861, per Lord Denman.

¹⁵⁰ *Bank of Columbia v. Patterson's Adm'r*, 7 Cranch, 299, 1 Cumming, Cas. Priv. Corp. 112, per Mr. Justice Story.

¹⁵¹ See *Topping v. Bickford*, 4 Allen (Mass.) 120, 1 Cumming, Cas. Priv. Corp. 118; *Bank of Columbia v. Patterson's Adm'r*, *supra*; *Goodwin v. Screw Co.*, 34 N. H. 378, 1 Cumming, Cas. Priv. Corp. 119; *Pixley v. Railroad Co.*, 33 Cal.

contract made by him in writing not under seal, or orally, within the scope of his authority and of the legitimate purposes of the corporation, will be binding as the contract of the corporation.¹⁵² And a corporation may, like a natural person, ratify any contract made by a person on its behalf, which it could have authorized him to make.¹⁵³ So, also, a corporation may be liable, like a natural person, on contracts implied, as a matter of fact, from corporate acts,¹⁵⁴ and on quasi contractual obligations, or contracts implied, as a matter of law, because of benefits conferred, or because of duties imposed, by law.¹⁵⁵

183, 1 Cumming, Cas. Priv. Corp. 121; Hand v. Coal Co., 143 Pa. St. 408, 22 Atl. 709; Lathrop v. Bank, 8 Dana (Ky.) 114. The seal of a corporation is not necessary to the validity of a power of attorney to confess judgment. Ford v. Hill (Wis.) 66 N. W. 115.

¹⁵² Bank of Columbia v. Patterson's Adm'r, supra. And see Mott v. Hicks, 1 Cow. (N. Y.) 513; Fleckner v. Bank, 8 Wheat. 338, 357. Australian Royal Mail Steam Nav. Co. v. Marzetti, 32 Eng. Law & Eq. 572; Muscatine Water Co. v. Muscatine Lumber Co., 85 Iowa, 112, 52 N. W. 108; Regents of University of Michigan v. Detroit Young Men's Soc., 12 Mich. 138; City of Selma v. Mullen, 46 Ala. 411; Board of Education of Illinois v. Greenebaum, 39 Ill. 609; Town of New Athens v. Thomas, 82 Ill. 259; B. S. Green Co. v. Blodgett, 159 Ill. 169, 42 N. E. 176; Christian Church of Wolcott v. Johnson, 53 Ind. 273; Fowler v. Bell (Tex. Civ. App.) 35 S. W. 822.

¹⁵³ Pixley v. Railroad Co., 33 Cal. 183, 1 Cumming, Cas. Priv. Corp. 121; Peterson v. City of New York, 17 N. Y. 450; Fister v. La Rue, 15 Barb. (N. Y.) 323. In this case it was said: "It is well settled, at least in this country, that where a person is employed for a corporation by one assuming to act in its behalf, and goes on and renders the services according to the agreement, with the knowledge of its officers, and without notice that the contract is not recognized as valid and binding, such corporation will be held to have sanctioned and ratified the contract, and be compelled to pay for the services according to the agreement. Having availed itself of the services, and received the benefits, it is bound in conscience to pay, and will not be heard to say that the original agreement was not made by a person legally authorized to contract."

¹⁵⁴ Pixley v. Railroad Co., 33 Cal. 183, 1 Cumming, Cas. Priv. Corp. 121; Goodwin v. Screw Co., 34 N. H. 378, 1 Cumming, Cas. Priv. Corp. 119; Cicotte v. Catholic Church, 60 Mich. 552, 27 N. W. 682; Proprietors of Canal Bridge v. Gordon, 1 Pick. (Mass.) 297; City of Selma v. Mullen, 46 Ala. 411; Town of New Athens v. Thomas, 82 Ill. 259.

¹⁵⁵ Bank of Columbia v. Patterson's Adm'r, 7 Cranch, 299, 1 Cumming, Cas. Priv. Corp. 112; Danforth v. President, etc., 12 Johns. (N. Y.) 227; Seagraves v. City of Alton, 13 Ill. 366; Trustees of Cincinnati Tp. v. Ogden, 5 Ohio, 28; Jefferys v. Gurr, 2 Barn. & Adol. 833.

If the charter of a corporation, or some statute applicable to it, expressly prescribes a certain mode or form for entering into contracts, that mode and form must be followed.¹⁵⁶ The provision, however, must be mandatory, and not merely directory.¹⁵⁷ Even where there is such a provision, and it is not complied with, the corporation may be liable. Thus, if it enters into a contract, but not in the form prescribed by its charter or a statute, and receives the consideration, it cannot always escape liability to pay therefor on the ground that the contract was not in the prescribed form, though it might have defeated a recovery so long as the contract remained wholly executory. In *Pixley v. Western Pac. R. Co.*,¹⁵⁸ the charter of a railroad company declared that no contract should be binding on the company unless in writing. The directors orally employed the plaintiffs to render services for the company, and, after the services were rendered, it was sought to defeat a recovery therefor because the contract was not in writing. The court held, however, that the charter, properly interpreted, only related to executory contracts, and did not exempt the company from liability to pay for the services after having had the benefit of them. "It may be," it was said, "that, while such contract remains executory on both sides, an action could not be maintained by either party to enforce it; but where one of the contracting parties has completely performed it on his part, and thereby rendered to the other the consideration stipulated, the party, having received the consideration promised, cannot be permitted to escape liability on the naked letter of the statute, because the meaning of the law is not such as to afford immunity from liability in such a case."¹⁵⁹ So, in North Carolina, where the Code provides that contracts by corporations for over \$100 must be in writing, it is held that the provision does

¹⁵⁶ *Head v. Insurance Co.*, 2 Cranch, 127; *Bissell v. Spring Valley Tp.*, 110 U. S. 162, 3 Sup. Ct. 555. As that all contracts shall be in writing or print, and signed by a particular officer or officers. *Topping v. Blackford*, 4 Allen (Mass.) 120, 1 Cumming, Cas. Priv. Corp. 118; *Pixley v. Railroad Co.*, 33 Cal. 183, 1 Cumming, Cas. Priv. Corp. 121.

¹⁵⁷ *Southern Life Ins. & Trust Co. v. Lanier*, 5 Fla. 110; *Witte v. Fishing Co.*, 2 Conn. 260; *Bulkley v. Fishing Co.*, Id. 252.

¹⁵⁸ 33 Cal. 183, 1 Cumming, Cas. Priv. Corp. 121.

¹⁵⁹ And see *Fister v. La Rue*, 15 Barb. (N. Y.) 323.

not apply to executed contracts.¹⁶⁰ If, under such a statute, the verbal contract is executed in part only, the corporation cannot be compelled to continue the contract, but is liable for what it has received by the part performance.¹⁶¹

Contracts under Seal.

A seal is said by Lord Coke to be wax, with an impression; and no doubt anciently wax was the only substance used, but it is no longer essential. The impression may be made on a wafer attached to the instrument, or any other substance sufficiently tenacious to adhere, and capable of receiving an impression. It is therefore held sufficient if the impression is made on the paper itself on which the instrument is written. It need not be on a separate substance attached to the paper.¹⁶² In some states, statutes have been passed making a scrawl or scroll sufficient, and in some this has been held sufficient independently of any statute; but by the weight of authority, at common law, an impression is essential;¹⁶³ and in the case of a corporation, of course, it must be by the duly-authorized agent of the corporation. It has been held that a fac simile of the seal of a corporation, printed upon blank forms of obligations, prepared to be executed by the corporation, at the same time when the blanks were printed, and by the same agency, was not a seal at common law.¹⁶⁴

Where a corporation executes a contract or conveyance required to be under seal, the seal of the corporation must be affixed, and by an officer or agent duly authorized.¹⁶⁵ It is not necessary that it shall be affixed by the officer personally. In the case of a contract

¹⁶⁰ *Curtis v. Mining Co.*, 109 N. C. 401, 13 S. E. 944; *Clowe v. Product Co.*, 114 N. C. 304, 19 S. E. 153.

¹⁶¹ *Roberts v. Woodworking Co.*, 111 N. C. 432, 16 S. E. 415.

¹⁶² *Clark*, Cont. 74.

¹⁶³ *Id.*

¹⁶⁴ *Bates v. Railroad Co.*, 10 Allen (Mass.) 251.

¹⁶⁵ A deed of conveyance by a corporation must be executed in the corporate name and under the corporate seal. A corporation, like an individual, may adopt any seal which is convenient for the occasion. It must, however, be shown to have been so adopted, and it must be affixed as the seal of the corporation, and by an officer or agent duly authorized. *Danville Seminary v. Mott*, 136 Ill. 289, 28 N. E. 54. Seals of the agents who execute the instrument will not do. *Regents of University of Michigan v. Detroit Young Men's Soc.*, 12 Mich. 138.

under seal by a natural person, "if a stranger seal an instrument by the allowance, or commandment precedent, or agreement subsequent, of the person who is to seal it, that is sufficient."¹⁶⁶ The same is true of contracts under seal by corporations. Thus, where the corporate seal was affixed by a printer to the bonds of a corporation, by direction of its officers, and the officers afterwards adopted his act, and signed and issued the bonds, it was held that this was a sufficient sealing by the corporation.¹⁶⁷

In equity, omission of a seal does not always invalidate an instrument executed by a corporation, even in cases where it would be invalid at law. A mortgage by a corporation, for instance, may be a good equitable mortgage, though by the omission of the seal it is not good as a legal mortgage.¹⁶⁸

Where the deed of a corporation, signed by a person authorized to execute the same, recites that it is sealed with the corporate seal, it will be presumed that what purports to be a seal, placed after the person's name, was the seal of the corporation.¹⁶⁹

The mere fact that a deed has the seal of the corporation attached does not make it the deed of the corporation, unless the seal was affixed by some one duly authorized. There is a presumption, however, that it was so affixed, but the presumption is not conclusive, and may always be rebutted.¹⁷⁰ In the absence of express requirement to that effect, it is not necessary that the deed of a corpora-

¹⁶⁶ Cruise, Dig. tit. 32, c. 2, § 55.

¹⁶⁷ Royal Bank of Liverpool v. Grand Junction Railroad & Depot Co., 100 Mass. 444, 1 Cumming, Cas. Priv. Corp. 131.

¹⁶⁸ Allis v. Jones, 45 Fed. 148.

¹⁶⁹ Benbow v. Cook, 115 N. C. 324, 20 S. E. 453; Jacksonville, M. P. Ry. & Nav. Co. v. Hooper, 160 U. S. 514, 16 Sup. Ct. 379.

¹⁷⁰ Koehler v. Iron Co., 2 Black, 715. It was held in this case that, where neither the president nor the secretary pro tem., who signed a mortgage on behalf of a corporation, nor the regular secretary, who was the regular custodian of the seal, had any knowledge of the way in which the mortgage became sealed, the burden of proof was thrown upon the party seeking to enforce it to show the circumstances under which the seal was affixed, and that it was rightfully and properly done. See, also, Bliss v. Irrigation Co., 65 Cal. 502, 4 Pac. 507; Andres v. Fry (Cal.) 45 Pac. 534; Gorder v. Canning Co., 36 Neb. 548, 54 N. W. 830; Yanish v. Fuel Co. (Minn.) 66 N. W. 198; Leggett v. Banking Co., 1 N. J. Eq. 541.

tion, executed by an agent under authority of a vote at a stockholders' or directors' meeting, shall recite the vote.¹⁷¹

Effect of Seal.

It has been said that a sealed instrument conclusively imports a consideration, and therefore the holders of corporate bonds may maintain an action thereon, though they were delivered gratuitously.¹⁷² This dictum, however, cannot be supported. The seal on a contract of a corporation has no greater effect than a seal on a natural person's contract. The seal does not import a consideration at all at common law. It merely renders a consideration unnecessary.¹⁷³ Where there was in fact a consideration, the seal does not prevent a natural person from defeating an action on his contract by showing that the consideration was illegal or immoral.¹⁷⁴ So, in the case of corporate contracts under seal, want of consideration may be shown, or the consideration may be shown to have been such that the corporation had no authority to enter into the contract. "Although the agreement be under seal," said Lord Campbell on this point, "we may examine to see whether there was any, and what, consideration for the contract to pay money, when we are to determine whether the contract was or was not ultra vires."¹⁷⁵

As we have pointed out, corporate bonds may be negotiable instruments, in which case inquiry into the consideration would not be permitted, in order to defeat liability to a bona fide holder.¹⁷⁶

¹⁷¹ *McDaniels v. Manufacturing Co.*, 22 Vt. 274.

¹⁷² *Foster, J.*, in *Royal Bank of Liverpool v. Grand Junction Railroad & Depot Co.*, 100 Mass. 444, 445, 1 Cumming, Cas. Priv. Corp. 131.

¹⁷³ *Anson*, Cont. 49; *Clark*, Cont. 72, 82.

¹⁷⁴ *Clark*, Cont. 83.

¹⁷⁵ *Mayor, etc., of City of Norwich v. Norfolk Ry. Co.*, 4 El. & Bl. 443.

¹⁷⁶ *Ante*, p. 146.

CHAPTER VI.

POWERS AND LIABILITIES OF CORPORATIONS (Continued).

- 62. Effect of Ultra Vires Act—In General.
- 63. A Corporation May Exceed Its Powers.
- 64. Assent of Shareholders.
- 65, 66. Ultra Vires Conveyances of Land or Transfers of Personalty.
- 67. Ultra Vires Contracts.
- 68. Illegal Contracts.

EFFECT OF ULTRA VIRES ACT.

62. If a corporation performs or threatens to perform an act which is ultra vires, but not otherwise unlawful—
- (a) The state may, when the act is done, maintain proceedings against it to forfeit its charter for misuser.
 - (b) A stockholder or member may, where the act is threatened, maintain a bill in equity to enjoin the corporation from performing it. He may sue to enjoin performance of an ultra vires contract which the corporation has already entered into, provided it is not binding on the corporation under the rules hereafter shown.
 - (c) As to the effect of an ultra vires conveyance to or by a corporation, and as to the circumstances under which an action may be maintained on an ultra vires contract, the authorities, as will be seen, are conflicting.

There is much conflict in the cases as to the effect of a corporation's ultra vires acts and contracts, and as to the circumstances under which they may give rise to actions. It is not possible to state general rules that will apply in all the states. There are some rules which are universally recognized, while as to others there is a direct

conflict. On some points there are decisions by the same court which cannot well be reconciled. All that can be done in a work of this character is to group the decisions as far as possible, and show the different positions the courts have taken.

All the authorities agree that where a corporation enters into an ultra vires contract, or performs an ultra vires act, though the contract or act is only unlawful because it is unauthorized, the state may, if the act is sufficiently flagrant to justify it, maintain proceedings directly against the corporation to enforce a forfeiture of its charter for the misuser of power. This question will be fully considered hereafter.¹

The authorities also agree that, under certain conditions, a bill in equity may be maintained by a stockholder or member against the corporation to enjoin it from entering into an ultra vires contract, or from performing a threatened ultra vires act; and such a bill may also be maintained to prevent it from performing an ultra vires contract,² unless the contract is enforceable against it, under the doctrines which we shall presently explain, notwithstanding its ultra vires character. The fact that a stockholder is not injured by an ultra vires contract of the corporation, to which all the other stockholders have consented, does not prevent him from maintaining a suit to enjoin its performance.³

As to the effect of an ultra vires conveyance to or by a corporation, as between the parties, and as to whether an action may be maintained by or against a corporation under an ultra vires contract, the authorities are conflicting, as we shall see in the following sections.

SAME—A CORPORATION MAY EXCEED ITS POWERS.

63. By the term "power," as applied to corporations, is meant "authority." It is possible for a corporation to exceed its powers and do unauthorized acts, and out of such acts rights and liabilities may arise.

¹ Post, p. 237.

² Post, p. 389.

³ *Byrne v. Manufacturing Co.*, 65 Conn. 336, 81 Atl. 833.

When it is said that a corporation has such "powers" only as are expressly or impliedly conferred upon it by the legislature which created it, it is not meant that it is unable to do any act in excess of the powers conferred, but simply that it has no authority or right to do such an act. It may, in fact, exceed its powers, and rights and liabilities may arise out of its unauthorized or "ultra vires" acts. In this respect it is like a natural person. Like a natural person, it may do wrong.⁴ If it were otherwise, it could not become liable for a tort, nor could it be prosecuted for a misdemeanor, such as the maintenance of a nuisance; and it is perfectly well settled, as we shall see, that it may be civilly liable for a tort,⁵ and criminally responsible for misdemeanor.⁶ Nor could it ever become liable to forfeiture of its charter for a violation thereof.⁷ So, as we shall see, a corporation may, under some circumstances, incur liability by reason of a contract entered into in excess of its powers.⁸ "Corporations, like natural persons, have power and capacity to do wrong. They may, in their dealings and contracts, break over the restraints imposed upon them by their charters; and when they do so their exemption from liability cannot be claimed on the mere ground that they have no attributes or faculties which render it possible for them thus to act." ⁹

This point was discussed in *Bissell v. Michigan Southern & N. I. R. Cos.*¹⁰ It was contended in that case that if the proper officers of a corporation enter into a contract or transaction which is not within the authority of the corporation, the transaction cannot be considered as in any sense that of the corporation, but is, in legal contemplation, that of the officers personally; in other words, that a corporation cannot exceed its powers, and that for this reason it cannot, under any conceivable circumstances, be held liable on an ultra vires contract or transaction, the officers alone being liable. Comstock,

⁴ See *Salt Lake City v. Hollister*, 118 U. S. 256, 6 Sup. Ct. 1055, 2 Cumming, Cas. Priv. Corp. 107.

⁵ Post, p. 193.

⁶ Post, p. 197.

⁷ Post, p. 237.

⁸ Post, p. 170; *Bissell v. Railroad Cos.*, 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 187; *Life & Fire Ins. Co. v. Mechanic Fire Ins. Co.*, 7 Wend. (N. Y.) 81.

⁹ *Wright v. Hughes*, 119 Ind. 324, 21 N. E. 907.

¹⁰ 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 187.

C. J., in repudiating this reasoning, said: "In this view these artificial existences are cast in so perfect a mold that transgression and wrong become impossible. The acts and dealings of a corporation, done and transacted in its name and behalf by its board of directors, vested with all its powers, are, unless justified by its charter, according to this reasoning, the acts and dealings of the individuals engaged in them, and for which they alone are responsible. But such, I apprehend, is not the nature of these bodies. Like natural persons, they can overleap the legal and moral restraints imposed upon them; in other words, they are capable of doing wrong. To say that a corporation has no right to do unauthorized acts is only to put forth a very plain truism; but to say that such bodies have no power or capacity to err is to impute to them an excellence which does not belong to any created existences with which we are acquainted. The distinction between power and right is no more to be lost sight of in respect to artificial than in respect to natural persons." In another case, where a similar contention was made, it was said by Sutherland, J., in refuting the doctrine: "This would be a most convenient distinction for corporations to establish,—that every violation of their charter, or assumption of unauthorized power on the part of their officers, although with the full approbation of their directors, is to be considered the act of the officers, and is not to prejudice the corporation itself. There would be no possibility of ever convicting a corporation of exceeding its powers, and thereby forfeiting its charter, or incurring any other penalty, if this principle could be established."¹¹

SAME—ASSENT OF SHAREHOLDERS.

64. An ultra vires contract, which is not binding upon the corporation, cannot be made binding by the assent or ratification of all the shareholders.

We shall see that in some jurisdictions ultra vires contracts may bind the corporation in certain cases on the principle of estoppel. Ordinarily, however, an ultra vires contract is null and void, and if this is the case it cannot be rendered binding upon the corporation

¹¹ Life & Fire Ins. Co. v. Mechanic Fire Ins. Co., 7 Wend. (N. Y.) 81.

by the assent or ratification of all the shareholders. If the contract is unauthorized by the charter, and illegal, it has been said "it is unnecessary to consider the effect of dissentient shareholders; for, if the company is a corporation only for a limited purpose, and a contract * * * is not within their authority, the assent of all the shareholders to such a contract, though it may make them all personally liable to perform such contract, will not bind them in their corporate capacity, or render liable their corporate funds."¹² —

**SAME—ULTRA VIRES CONVEYANCES OF LAND, OR
TRANSFERS OF PERSONALTY.**

65. An ultra vires conveyance of land to or by a corporation, which has the power to take and convey, but which in the particular instance has done so for an unauthorized purpose, is not void, but vests the title in the grantee. But, if there is no power at all to take or convey land, the conveyance is absolutely void. The same rule applies to transfers of personal property.

66. When the title to property which it has no authority to hold has not vested in the corporation, the courts will not aid it to acquire the title.

Where a corporation, having the power to acquire and hold land for certain purposes only, takes a conveyance of land for a purpose not authorized, or takes more land than it is authorized to hold, the conveyance is not absolutely void. The state may proceed directly against it for exceeding the powers conferred upon it, but the question is solely between it and the state. Neither the grantor nor any other private individual can attack the conveyance in a suit by or against the corporation to recover the land. So long as the state remains inactive, no one can complain; for, as was said

¹² Per Jervis, C. J., in *East Anglian Ry. Co. v. Eastern Counties Ry. Co.*, 11 C. B. 775, 1 Cumming, Cas. Priv. Corp. 142. And see *Directors, etc., of Ashbury Railway Carriage & Iron Co. v. Riche*, L. R. 7 H. L. 653, 1 Cumming, Cas. Priv. Corp. 152; *Thomas v. Railroad Co.*, 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164; *Germania Safety-Vault & Trust Co. v. Boynton*, 19 C. C. A. 118, 71 Fed. 797.

in a California case, it would lead to infinite embarrassments if in suits by corporations to recover possession of their property inquiries were permitted as to the necessity of such property for the purposes of their incorporation, and the title made to rest upon the existence of that necessity.¹³ If a corporation is absolutely prohibited from acquiring or holding land, and not merely restricted in the purposes for which it may do so, or as to the amount, a conveyance to it is absolutely void, and the objection, therefore, may be raised, not only by the state in a proceeding against the corporation, but also by the grantor, or any other private individual, collaterally, as in a suit by or against the corporation to recover the land.¹⁴

In *Case v. Kelly*¹⁵ a clear distinction was made by the supreme court of the United States between cases in which the title to land, which a corporation has no power to hold, has vested in it, and cases in which the title has not vested in it, and the corporation seeks the

¹³ *Natoma Water & Mining Co. v. Clarkin*, 14 Cal. 544. And see *Leazure v. Hillegas*, 7 Serg. & R. (Pa.) 313, 1 Cumming, Cas. Priv. Corp. 85; *Ayers v. Banking Co.*, L. R. 8 P. O. 548, 2 Cumming, Cas. Priv. Corp. 20; *Hough v. Land Co.*, 73 Ill. 23, 1 Cumming, Cas. Priv. Corp. 80; *Barnes v. Suddard*, 117 Ill. 237, 7 N. E. 477; *Banks v. Poitiaux*, 8 Rand. (Va.) 136, 15 Am. Dec. 706; *Bone v. Canal Co.* (Pa. Sup.) 5 Atl. 751; *Hamsher v. Hamsher*, 132 Ill. 273, 23 N. E. 1123; *Fayette Land Co. v. Louisville & N. R. Co.* (Va.) 24 S. E. 1016; *Jones v. Habersham*, 107 U. S. 174, 2 Sup. Ct. 336; *Barrow v. Turnpike Co.*, 9 Humph. (Tenn.) 304; *Mallett v. Simpson*, 94 N. C. 87; *Hanson v. Little Sisters of the Poor*, 79 Md. 434, 32 Atl. 1052; *Gilbert v. Hole*, 2 S. D. 164, 49 N. W. 1; *American Mortg. Co. of Scotland v. Tennille*, 87 Ga. 28, 13 S. E. 158; *Long v. Railway Co.*, 91 Ala. 519, 8 South. 706. It has been held, however, that where property is given by will to a corporation, which has no capacity to take or hold it, or whose capacity to take or hold is limited by its charter or by the general statute law, the bequest or devise will be invalid in so far as it exceeds the limit, and that the objection may be raised by any person interested under the will. *Starkweather v. Bible Soc.*, 72 Ill. 50; *Wood v. Hammond*, 16 R. I. 98, 17 Atl. 324; *Cromie's Heirs v. Society*, 3 Bush (Ky.) 365; *Chamberlain v. Chamberlain*, 43 N. Y. 424; *In re McGraw's Estate*, 45 Hun, 854, affirmed 111 N. Y. 66, 19 N. E. 233, 2 Cumming, Cas. Priv. Corp. 22. But see, contra, where the devise is merely of more land than the corporation is permitted to hold, *Hanson v. Little Sisters of the Poor*, 79 Md. 434, 32 Atl. 1052; *Jones v. Habersham*, 107 U. S. 174, 2 Sup. Ct. 336.

¹⁴ See *Hayward v. Davidson*, 41 Ind. 212; *Carroll v. City of East St. Louis*, 67 Ill. 568.

¹⁵ 133 U. S. 21, 10 Sup. Ct. 216, 1 Cumming, Cas. Priv. Corp. 106.

aid of the court to acquire title; and it was held that in the latter case the court should not aid the corporation. In the case at bar, land had been donated to a railroad company for purposes not authorized by its charter, and conveyed to officers of the company. A receiver of the company brought suit to charge them as trustees for the company, and to recover the land. It was held that the suit could not be maintained. "We need not stop here," said the court, "to inquire whether this company can hold title to lands which it is impliedly forbidden by its charter to do, because the case before us is not one in which the title to the lands in question has ever been vested in the company, or attempted to be so vested. The company is plaintiff in this action, and is seeking to obtain the title to such lands. It has no authority by the statute to receive such title and to own such lands, and the question here is, not whether the courts would deprive it of such lands if they had been conveyed to it, but whether they will aid it to violate the law, and obtain a title which it has no power to hold. We think the questions are very different ones, and that, while a court might hesitate to declare the title to lands received already, and in the possession and ownership of the company, void on the principle that they had no authority to take such lands, it is very clear that it will not make itself the active agent in behalf of the company in violating the law, and enabling the company to do that which the law forbids."

The rules above stated apply also to ultra vires transfers of personal property and assignments of choses in action to or by a corporation. If a corporation purchases or sells personal property, and possession is delivered, third persons cannot dispute the title under the transfer, and contend that the property remains in the seller, on the ground that the corporation had no power to take and hold or to transfer the same. Nor can the purchaser of property from a corporation defend an action on a note given to the corporation for the price, on the ground that the corporation had no power to hold the property.¹⁶ The same is true where a corporation purchases a note, in excess of its powers. The note is valid, and the

¹⁶ See *Ryers v. South Australian Banking Co.*, L. R. 3 P. C. 548, 2 Cumming, Cas. Priv. Corp. 20; *Edwards v. Fairbanks*, 27 La. Ann. 449; 2 Mor. Corp. § 712; *Holmes & Griggs Manuf'g Co. v. Holmes & Wessell Metal Co.*, 53 Hun, 52, 5 N. Y. Supp. 937; *Rutland & B. R. Co. v. Proctor*, 29 Vt. 93.

maker, when sued thereon by the corporation, cannot defeat the action by alleging that the purchase was ultra vires.¹⁷

SAME—ULTRA VIRES CONTRACTS.

67. On the question whether, and under what circumstances, an action will lie on an ultra vires contract, the authorities are in direct conflict, and there is much confusion in the cases. The different positions which have been taken by the courts may be stated thus:

- (a)** Some of the courts hold that a contract by a corporation which is objectionable only because it is ultra vires or unauthorized is on that ground alone illegal and void, as being contrary to public policy, and that, as a rule, no action can be maintained upon it. But
 - (1)** Where the contract is not clearly ultra vires, but is so only because of facts or circumstances of which the other party has neither actual nor constructive notice, an action on the contract may be maintained by the other party against the corporation.
 - (2)** Some courts have held that contracts of corporations which they have no authority at all to make are void, but that contracts which are within the general scope of their powers, but which are in some particulars in excess of those powers, are valid, unless by reason of such excess they are against public policy.
 - (3)** A transaction, or contract, if severable, may be valid in part, though in part it is ultra vires.
 - (4)** A negotiable instrument executed or indorsed by a corporation is good as against it in the hands of a holder for value and without no-

¹⁷ *National Pemberton Bank v. Porter*, 125 Mass. 333, 28 Am. Rep. 235. But see ante, p. 141; *Farmers' & Mechanics' Bank v. Baldwin*, 23 Minn. 198.

tice, unless the corporation clearly had no power at all to execute or indorse such instruments.

- (5) Where either party has received benefits under the contract in the form of money, property, or services, an action quasi ex contractu or suit for an accounting may be maintained to recover therefor.
- (6) Equity will not grant a corporation affirmative relief against an ultra vires contract, unless it restores the consideration, if any, received by it.
- (7) If a corporation borrows money without authority, but applies it to the payment of valid debts, so that its liabilities are not increased, the lender, or holders of obligations or securities issued for the loan, will be subrogated in equity to the rights of the creditors of the corporation whose debts have been so paid.
- (b) Most courts hold that the contracts of a corporation which are objectionable only because they are ultra vires, are not so far illegal that no action can be maintained upon them, and that the plea of ultra vires should not prevail, whether interposed for or against the corporation, when it would be inequitable and unjust to allow it; as where the party seeking to enforce the contract has performed it on his part.

The Doctrine that an Ultra Vires Contract is Illegal and Void.

Some of the courts have held that the ultra vires contract of a corporation, though it is unlawful only because it is unauthorized, is nevertheless illegal and void on that ground alone, as any excess of its powers by a corporation is contrary to public policy.¹⁸

¹⁸ Franklin Co. v. Lewiston Inst. for Savings, 68 Me. 43, 1 Cumming, Cas. Priv. Corp. 343. "The contracts of corporations which are not authorized by their

According to this doctrine, most of the rules relating to unlawful agreements generally, like immoral agreements and agreements in restraint of trade,¹⁹ apply to ultra vires contracts by a corporation; and no action can be maintained on such a contract, either by or against the corporation, unless the case falls within one of the exceptions hereafter mentioned. So long as the contract is wholly executory on both sides, there is no question as to the correctness of the rule that no action can be maintained upon it.²⁰ These courts, however, go further than this. They hold that the fact that the other party has incurred expenses or sustained losses, or even fully performed on his part, on the faith of the corporation's ultra vires promise, cannot render the corporation liable on the contract itself, except as hereafter shown.²¹ And of course, under this doctrine,

charters are illegal, because they are made in contravention of public policy. * * * Although the unauthorized contract may be neither *malum in se* nor *malum prohibitum*, but, on the contrary, may be for some benevolent or worthy object,—as to build an almshouse or a college, or to purchase and distribute tracts or books of instruction,—yet, if it is a violation of public policy for corporations to exercise powers which have never been granted to them, such contracts, notwithstanding their praiseworthy nature, are illegal and void.” Per Selden, J., in *Bissell v. Railroad Co.*, 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 202.

¹⁹ Clark, Cont. 470–500.

²⁰ *Nassau Bank v. Jones*, 95 N. Y. 115, 1 Cumming, Cas. Priv. Corp. 293.

²¹ See opinion of Selden, J., in *Bissell v. Railroad Co.*, 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 202 (collecting cases); *Davis v. Railroad Co.*, 131 Mass. 258, 1 Cumming, Cas. Priv. Corp. 173 (but see *Slater Woollen Co. v. Lamb*, 143 Mass. 420, 9 N. E. 823, 1 Cumming, Cas. Priv. Corp. 260); *East Anglian Rys. Co. v. Eastern Counties Ry. Co.*, 11 O. B. 775, 1 Cumming, Cas. Priv. Corp. 142; *Directors, etc., of Ashbury Railway Carriage & Iron Co. v. Riche*, L. R. 7 H. L. 653, 1 Cumming, Cas. Priv. Corp. 152; *Pearce v. Railroad Co.*, 21 How. 441, 1 Cumming, Cas. Priv. Corp. 146; *Thomas v. Railroad Co.*, 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164, W. D. Smith, Cas. Corp. 132, Shep. Cas. Corp. 70; *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148, W. D. Smith, Cas. Corp. 129, Shep. Cas. Corp. 75; *Northwestern Union Packet Co. v. Shaw*, 37 Wis. 655, 1 Cumming, Cas. Priv. Corp. 245; *Straus v. Insurance Co.*, 5 Ohio St. 59; *Central Transp. Co. v. Pullman's Palace Car Co.*, 139 U. S. 24, 11 Sup. Ct. 478; *Miller v. Insurance Co.*, 92 Tenn. 167, 21 S. W. 39; *Buckeye M. & F. Co. v. Harvey*, 92 Tenn. 115, 20 S. W. 427; *Bacon v. Insurance Co.*, 31 Miss. 116; *Chewacla Lime Works v. Dismukes*, 87 Ala. 344, 6 South. 122; *Miners' Ditch Co. v. Zellerbach*, 37 Cal. 543; *Albert v. Bank*, 1 Md. Ch. Dec. 407; *Abbott v. Packet Co.*, Id. 542. Thus, where two railroad companies, in excess of their powers, con-

performance by the corporation would not render the other party liable.²² We are speaking here only of cases in which the action is brought directly on the contract. Actions quasi ex contractu in disaffirmance of the contract may be maintained.²³ Not only is the defense of ultra vires available to the corporation in an action by the other party on the contract, but it is also available to the other party in an action by the corporation. The contract, according to the doctrine of these cases, being wholly null and void, cannot be made the foundation of an action by either party.²⁴

"The reasons," said Mr. Justice Gray, "why a corporation is not liable upon a contract ultra vires,—that is to say, beyond the powers conferred upon it by the legislature, and varying from the objects of its creation, as declared in the law of its organization,—are: (1) The interests of the public that the corporation shall not transcend the powers granted; (2) the interest of the stockholders that the capital shall not be subjected to the risk of enterprises not contemplated by the charter, and therefore not authorized by the stockholders in subscribing for the stock; (3) the obligation of every one entering into a contract with a corporation to take notice of the legal limits of its powers."²⁵

Same—Ignorance of Ultra Vires Character of Transaction.

Even in those states where the courts hold ultra vires contracts illegal and void, they make an exception to the rule where the party

consolidated, and as a consolidated company purchased property in excess of their powers, and gave notes therefor, it was held that an indorsee of the notes, who had notice of the circumstances under which they were given, could not maintain an action against the corporations thereon. *Pearce v. Railroad Co.*, supra. So where a corporation purchased and received property which it was not authorized to purchase or receive, it was held that an action would not lie against it for the price. *Downing v. Road Co.*, supra. And where a railroad company and a manufacturing company joined in an ultra vires subscription to contribute to defray the expenses of a festival, and the festival was held, and the expenses paid by the committee, it was held that the committee could not maintain an action on the subscription. *Davis v. Railroad Co.*, supra.

²² *Oregon Ry. & Nav. Co. v. Oregonian Ry. Co.*, 130 U. S. 1, 9 Sup. Ct. 409.

²³ *Post*, p. 177.

²⁴ *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148, W. D. Smith, Cas. Corp. 129, Shep. Cas. Corp. 75.

²⁵ *Pittsburgh, O. & St. L. Ry. Co. v. Keokuk & H. Bridge Co.*, 131 U. S. 371. 9 Sup. Ct. 770.

dealing with the corporation did not know, and is not chargeable with knowledge of, the ultra vires nature of the contract into which he entered. The cases are virtually agreed that, if the officers of a corporation make a contract with a man in regard to matters apparently within the powers of the corporation, but which, upon proof of extrinsic facts, of which he had no notice, and of which he is not chargeable with notice, is shown to have been ultra vires, the corporation may be held liable, unless it may and does avoid liability by taking timely steps to prevent loss or damage to the other party.²⁶ Thus, if a corporation empowered to build and operate a certain line of railroad should purchase rails for the purpose of building another line, or for the purpose of speculating in them, without the knowledge of the vendor, the corporation could be held on the contract.²⁷ So, if a corporation, which is limited by its charter as to the amount of indebtedness it may incur, should purchase property, and in doing so exceed that amount, the seller, being ignorant of the amount of the company's indebtedness at the time of the purchase, could hold it on the contract.²⁸

It is held, however, that where a corporation is created, and its powers conferred by a public act, a man who enters into a contract with it, which is clearly in excess of its powers as shown by the act, cannot enforce the contract, for he is chargeable with knowledge of public laws, and therefore of the powers of the corporation.²⁹ Thus it has been held that if a corporation, not being authorized by its charter, enters into a contract of guaranty or suretyship, this is clearly in excess of its powers, and that the other party is chargeable with knowledge of this fact, and cannot hold it liable.³⁰

Same—Unauthorized Exercise of Authorized Powers.

Some of the courts have made this distinction: That contracts of corporations which they have no authority at all to make are void and unenforceable; but that contracts which are within the general

²⁶ *Miners' Ditch Co. v. Zellerbach*, 37 Cal. 543; *Lucas v. Transfer Co.*, 70 Iowa, 542, 30 N. W. 771; *Bissell v. Railroad Co.*, 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 196, per Comstock, C. J.; *Boyce v. Coal Co.*, 37 W. Va. 73, 16 S. E. 501.

²⁷ Dictum in *Lucas v. Transfer Co.*, supra.

²⁸ *Humphrey v. Association*, 50 Iowa, 607.

²⁹ *Lucas v. Transfer Co.*, 70 Iowa, 542, 30 N. W. 771.

³⁰ *Lucas v. Transfer Co.*, supra.

scope of their powers, but which are, in some particulars, in excess of those powers, are valid, unless by reason of such excess they are against public policy. The Wisconsin court applied this rule to a case in which a corporation had exceeded its powers in lending money for two years, instead of one, and upon note and mortgage, instead of upon bond and mortgage, and held that the corporation could maintain an action upon the securities.³¹ The same principle was applied where a bank limited by its charter to taking ten per cent. interest on loans discounted a note at twelve per cent. It was held that the loan was valid as to ten per cent. interest, and void only as to the excess.³² On this point, however, the cases are conflicting.³³

Same—Severable Transaction.

A contract or transaction by a corporation, if severable, may be valid in so far as it is within the powers of the corporation, though in part it is ultra vires. Thus, if a railroad company, having implied authority to issue bonds in order to raise money for its business, but without authority to execute a mortgage on its property, issues bonds secured by a mortgage, the invalidity of the mortgage cannot be set up to defeat a recovery on the bonds.³⁴ So where a railroad or other corporation has express authority to mortgage its property, a mortgage executed by it, covering both its property and its franchise, will not be avoided as to the property by the fact that there was no authority to mortgage the franchise.³⁵

Same—Negotiable Bills and Notes—Bonds.

A negotiable bill or note accepted, made, or indorsed by a corporation, in excess of the powers conferred upon it by its charter, stands, of course, upon exactly the same footing as other contracts, as between the original parties. Difficult questions arise in cases where the instrument has passed into the hands of one who claims to be a bona fide holder for value. These rules seem to be well settled in

³¹ *Germantown Farmers' Mut. Ins. Co. v. Dhein*, 43 Wis. 420. And see *Rock River Bank v. Sherwood*, 10 Wis. 230; *Littlewort v. Davis*, 50 Miss. 403.

³² *Rock River Bank v. Sherwood*, supra.

³³ *Bank of Chillicothe v. Swayne*, 8 Ohio, 257.

³⁴ *Philadelphia & S. R. Co. v. Lewis*, 33 Pa. St. 33. And see *Pittsburgh, C. & St. L. Ry. Co. v. Keokuk & H. Bridge Co.*, 131 U. S. 371, 9 Sup. Ct. 770.

³⁵ *Gloninger v. Railroad Co.*, 139 Pa. St. 13, 21 Atl. 211.

most jurisdictions. If the execution or indorsement of a negotiable instrument by a corporation is obviously foreign to the purposes of its charter, such an instrument is void into whosoever's hands it may come, for every person is chargeable with notice of its ultra vires character; but if a corporation is of such a character that it may have occasion to execute or to take and indorse such instruments in the conduct of its business, and it accepts a bill or executes a note, or indorses a bill or note, for a purpose that is foreign to its objects, as where it gives its paper as an accommodation, or in payment for property which it has no authority to purchase, the instrument will be binding in the hands of a purchaser for value and without notice.⁸⁶ If the purchaser had notice in fact, or if the circumstances were such as to put him on inquiry, and charge him with notice, of the ultra vires character of the transaction, he cannot recover, unless under rules hereafter shown the original holder could recover.⁸⁷ An indorser of the note of a corporation which is expressly prohibited from issuing notes, though the note is negotiable in form, is not liable thereon.⁸⁸

As we have seen, the bonds issued by a corporation, and the coupons attached thereto, will be regarded as negotiable instruments, and as subject to the rules of law relating to such instruments, if it appears from the form in which they were issued, and the mode of giving them circulation, that they were intended to have this char-

⁸⁶ Norton, Bills & N. 211-215; Monument Nat. Bank v. Globe Works, 101 Mass. 57, 1 Cumming, Cas. Priv. Corp. 315; National Park Bank v. German-American M. W. & S. Co., 116 N. Y. 281, 22 N. E. 567, 1 Cumming, Cas. Priv. Corp. 318, Shep. Cas. Corp. 132; National Bank v. Young, 41 N. J. Eq. 531, 7 Atl. 488; Ex parte Estabrook, Fed. Cas. No. 4,534; Ridgway v. Bank, 12 Serg. & R. (Pa.) 256; Southern Loan Co. v. Morris, 2 Pa. St. 175; McIntire v. Preston, 5 Gilman (Ill.) 48; Auerbach v. Mill Co., 28 Minn. 291, 9 N. W. 799; Jacobs Pharmacy Co. v. Southern Banking & Trust Co. (Ga.) 25 S. E. 171; Marshall Nat. Bank v. O'Neal (Tex. Civ. App.) 34 S. W. 344.

⁸⁷ National Park Bank v. German-American M. W. & S. Co., *supra*. In this case a corporation without authority indorsed promissory notes for the accommodation of the maker, who himself had them discounted. It was held that the fact that the maker had them discounted for his own benefit, being unexplained, was notice to the discounter that the indorsement was not in the usual course of business, but merely for the accommodation of the maker, and that the discounter, therefore, could not hold the corporation liable. And see Price v. Coal Co. (Ky.) 32 S. W. 267.

⁸⁸ Southern Loan Co. v. Morris, 2 Pa. St. 175.

acter. And they will be subject to the rules protecting bona fide purchasers of negotiable instruments.³⁹

Same—Actions Quasi ex Contractu—Suit in Equity for Accounting.

If a corporation has received money or property or the benefit of services under an ultra vires contract, the courts are virtually agreed that it may be compelled to refund the value of that which it has actually received in an action quasi ex contractu, or, in a proper case, in a suit for an accounting.⁴⁰ Thus, where a manufacturing company purchased materials for the purpose of selling them again on speculation, it was held that the seller, after delivering part and repudiating the contract, could recover the value of the materials delivered. "It is to be observed," said the court, "that the contract, though void in law, involved no element of criminality, and nothing of an immoral nature. The case is not, therefore, one in which the law will leave the parties without redress for the consequences of criminal or immoral action. The plaintiff has a right to sell her manufacture, and to be paid for it; the defendant has received something of value from her, and there is manifest equity in its being required to make payment, notwithstanding it exceeded its powers in the purchase."⁴¹ And if money is paid by a corporation under a contract which is merely ultra vires, and not otherwise lawful, it may recover the money in an action for money had and received. Thus, where a transportation company entered into an ultra vires contract to purchase wheat, and paid part of the price, it was held that on failure

³⁹ Ante, p. 146, and cases there cited.

⁴⁰ *Day v. Buggy Co.*, 57 Mich. 146, 23 N. W. 628, and 1 Cumming, Cas. Priv. Corp. 261; *Northwestern Union Packet Co. v. Shaw*, 37 Wis. 655, 1 Cumming, Cas. Priv. Corp. 245; *Davis v. Railroad Co.*, 131 Mass. 258, 1 Cumming, Cas. Priv. Corp. 173; *Morville v. Tract Soc.*, 123 Mass. 129; *White v. Bank*, 22 Pick. (Mass.) 181, 1 Cumming, Cas. Priv. Corp. 239; *New Castle Northern R. Co. v. Simpson*, 23 Fed. 214; *Logan County Nat. Bank v. Townsend*, 139 U. S. 67, 11 Sup. Ct. 496; *In re Cork & Y. Ry. Co.*, 4 Ch. App. 748, 1 Cumming, Cas. Priv. Corp. 265; *Nashua & L. R. Corp. v. Boston & L. R. Corp.*, 164 Mass. 222, 41 N. E. 268; *Anthony v. Machine Co.*, 16 R. I. 571, 18 Atl. 176; *Manville v. Mining Co.*, 17 Fed. 425; *Moore v. Tanning Co.*, 60 Vt. 459, 15 Atl. 114; *Manchester & L. R. R. v. Concord R. R.* (N. H.) 20 Atl. 383. And see *Paul v. City of Kenosha*, 22 Wis. 266; *Louisiana v. Wood*, 102 U. S. 204; *Brown v. City of Atchison*, 39 Kan. 37, 17 Pac. 465; *Humphrey v. Association*, 50 Iowa, 607.

⁴¹ *Day v. Buggy Co.*, supra.

of the other party to deliver the wheat the money could be recovered back by the corporation.⁴²

Same—Relief in Equity against Ultra Vires Contract.

Where a corporation has received the consideration for an ultra vires contract, and then comes into a court of equity asking to have the contract declared void, and to be restored to the rights which it parted with, the relief will not be granted unless the corporation restores the consideration which it has received. In *American Union Tel. Co. v. Union Pac. Ry. Co.*,⁴³ a railroad company, authorized also to construct and operate a telegraph line, leased the telegraph line to another without authority, and received the consideration. It afterwards brought suit in equity to set the lease aside, and recover possession of the property. Judge McCrary held that the relief would not be granted unless it returned the consideration which it had received.

If an ultra vires contract has been fully executed, neither party can maintain an action at law or a suit in equity to recover what he or it has parted with. Thus one who has sold, received payment for, and conveyed land to a corporation cannot sue to rescind the conveyance on the ground that the corporation had no power to purchase. Nor, under the same circumstances, could the corporation rescind the purchase and recover what it has paid.⁴⁴

Same—Borrowing Money—Subrogation of Lender.

In equity, if a corporation borrows money without authority, but applies it in whole or in part, directly or indirectly, to the payment of valid debts, the lender will not lose the money thus applied, but will be subrogated to the rights of the creditors of the corporation thus paid, and to that extent may enforce his claim against the corporation. And if for such loan the corporation, without authority, issues debentures or bonds, the holders of them will occupy the same position as the lender.⁴⁵ This doctrine depends on the fact that liabili-

⁴² *Northwestern Union Packet Co. v. Shaw*, *supra*.

⁴³ 1 McCrary, 188, 1 Fed. 745, and 1 Cumming, *Cas. Priv. Corp.* 284.

⁴⁴ *Long v. Railway Co.*, 91 Ala. 519, 8 South. 706.

⁴⁵ In *re Cork & Y. Ry. Co.*, 4 Ch. App. 748, 1 Cumming, *Cas. Priv. Corp.* 265. This and similar cases, said Sir G. M. Giffard, L. J., in *Re National Permanent Benefit Building Soc.*, 5 Ch. App. 300, 1 Cumming, *Cas. Priv. Corp.* 274, "were decided upon a principle recognized in old cases, beginning with *Marlow v. Pitfield*,

ties of the company are not increased, and it is not to be applied where the money borrowed does not go to pay valid debts of the company.⁴⁶ But it is applicable as well where the money is applied to the payment of debts accruing subsequent to the borrowing as when it is applied to debts then existing.⁴⁷ "The test is, has the transaction really added to the liabilities of the company? If the amount of the company's liabilities remains, in substance, unchanged, but there is merely for the convenience of payment a change of the creditor, there is no substantial borrowing in the result, so far as relates to the position of the company. Regarded in that light, it is consistent with the principle of equity that those who pay legitimate demands, which they are bound in some way or other to meet, and have had the benefit of other people's money, advanced to them for that purpose, shall not retain that benefit, so as, in substance, to make those other people pay their debts. I take that to be a principle sufficiently sound in equity; and if the result is that by the transaction which assumes the shape of an advance or loan, nothing is really added to the liabilities of the company, there has been no real transgression of the principle on which they are prohibited from borrowing."⁴⁸

The Doctrine Allowing a Recovery on an Ultra Vires Contract.

In New York, Illinois, Michigan, Indiana, and many other states, the doctrine that the ultra vires contracts of a corporation are so far contrary to the public policy and illegal that they cannot form the foundation of an action, except as heretofore shown, is repudiated as being unjust, and not founded upon any sound principle of public

1 P. Wms. 558, where there was a loan to an infant, and the money was spent in paying for necessities; and in another case of a more modern date, where there was money actually lent to a lunatic, and it went in paying expenses which were necessary for the lunatic. In such case it has been held that, although the party lending the money could maintain no action, yet, inasmuch as his money had gone to pay debts which would be recoverable at law, he could come into a court of equity, and stand in the place of those creditors whose debts had been so paid.

* * * It is a very clear and definite principle which ought not to be departed from." And see *Wenlock v. River Dee Co.*, 19 Q. B. Div. 155, 1 Cumming, Cas. Priv. Corp. 277, and 10 App. Cas. 354.

⁴⁶ In re National Permanent Benefit Building Soc., *supra*.

⁴⁷ *Wenlock v. River Dee Co.*, *supra*.

⁴⁸ Per Lord Selborne in *Blackburn Building Soc. v. Cunliffe*, 22 Ch. Div. 61, 71.

policy. And the doctrine in these states is, to use the language of the New York court in a leading case, that "the plea of ultra vires should not, as a general rule, prevail, whether it is interposed for or against the corporation, when it would not advance justice, but, on the contrary, would accomplish a legal wrong."⁴⁹ This is clearly the better doctrine, and is supported by the great weight of decision in this country. Want of authority, as was pointed out by Comstock, C. J., in a New York case, may render a contract void; but mere want of authority, without more, does not render a contract illegal, so that it can under no circumstances give rise to an action. Contracts are illegal either in respect to the consideration or the promise. Where both of these are lawful and right, the maxim "*Ex turpi causa non oritur actio*," can have no application. The incapacity of the contracting party, whether it be a corporation, an infant, a married woman, or a lunatic, has nothing to do with the legality of the contract. A promise by a corporation, therefore, founded on a lawful consideration, and to do that which in itself is lawful to be done, although not within the powers granted by its charter, and therefore ultra vires, is not illegal,⁵⁰ and there is no good reason why it should not be held that causes of action may arise out of it. "A transgression of this nature is a simple excess of power (using that word to express the rules of action prescribed in their charters, and by which they ought to regulate their conduct), but is not tainted with illegality, so as to avoid the contract or dealing on that ground. This proposition, it seems hardly necessary to repeat, is applied only to transactions which involve or contemplate no violation of the code of private or criminal law, but, on the contrary, are innocent and lawful in themselves."⁵¹

⁴⁹ *Whitney Arms Co. v. Barlow*, 63 N. Y. 62, 1 Cumming, Cas. Priv. Corp. 253; *Kadish v. Association*, 151 Ill. 531, 38 N. E. 236; *Portland L. & M. Co. v. City of East Portland*, 18 Or. 21, 22 Pac. 536. And cases cited in the following notes.

⁵⁰ Per Comstock, C. J., in *Bissell v. Railroad Co.*, 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 187, 193. Compare the opinion of Selden, J., in this case.

⁵¹ Per Comstock, C. J., in *Bissell v. Railroad Co.*, *supra*. It was further said: "The words 'ultra vires' and 'illegality' represent totally different and distinct ideas. It is true that a contract may have both of these defects, but it may also have one without the other. For example, a bank has no authority to engage in benevolent enterprises. A subscription, made by authority of the board of directors, and under the corporate seal, for the building of a church or college, or an

In accordance with this view, it is held in most states that, if a contract entered into by a corporation is objectionable merely because it is in excess of the powers conferred upon the corporation by its charter, not being otherwise contrary to law, and it has been so far performed or acted upon by one of the parties that it would be inequitable to hold the contract void, the other party cannot defeat an action brought on the contract itself by setting up the defense that it was ultra vires.⁵² Thus it has been held that if a corporation enters into an ultra vires contract to purchase goods, and the goods are delivered to it, so that it receives the benefit of the

almshouse, would be clearly ultra vires, but it would not be illegal. If every corporation should expressly assent to such an application of the funds, it would still be ultra vires, but no wrong would be committed, and no public interest violated. So a manufacturing corporation may purchase ground for a schoolhouse or a place of worship for the intellectual, religious, and moral improvement of its operatives; it may buy tracts and books of instruction for distribution among them. Such dealings are outside of the charter; but, so far from being illegal or wrong, they are in themselves benevolent and praiseworthy. So a church corporation may deal in exchange. This, although ultra vires, is not illegal, because dealing in exchange is, in itself, a lawful business, and there is no state policy in restraint of that business."

⁵² Bissell v. Railroad Co., 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 187; Parish v. Wheeler, 22 N. Y. 494, 2 Cumming, Cas. Priv. Corp. 58; Whitney Arms Co. v. Barlow, 63 N. Y. 62, 1 Cumming, Cas. Priv. Corp. 253; Holmes & Griggs Manuf'g Co. v. Holmes & Wessell Metal Co., 127 N. Y. 252, 27 N. E. 831; Denver Fire Ins. Co. v. McClelland, 9 Colo. 11, 9 Pac. 771, 1 Cumming, Cas. Priv. Corp. 227; Bradley v. Ballard, 55 Ill. 413, 1 Cumming, Cas. Priv. Corp. 249, W. D. Smith, Cas. Corp. 187, Shep. Cas. Corp. 68; Heims Brewing Co. v. Flannery, 187 Ill. 309, 27 N. E. 286; Day v. Buggy Co., 57 Mich. 151, 23 N. W. 628, 1 Cumming, Cas. Priv. Corp. 261; Carson City Sav. Bank v. Carson City El. Co., 90 Mich. 550, 51 N. W. 641; Dewey v. Railway Co., 91 Mich. 351, 51 N. W. 1063; Slater Woolen Co. v. Lamb, 143 Mass. 420, 9 N. E. 828, 1 Cumming, Cas. Priv. Corp. 260 (Semble); Camden & A. R. Co. v. May's Landing, etc., R. Co., 48 N. J. Law, 530, 7 Atl. 523; State Board of Agriculture v. Citizens' St. Ry. Co., 47 Ind. 407, 1 Cumming, Cas. Priv. Corp. 222; Chicago & A. Ry. Co. v. Derkes, 103 Ind. 520, 3 N. E. 239; Wright v. Hughes, 119 Ind. 324, 21 N. E. 907; City of Corpus Christi v. Central Wharf & Warehouse Co., 8 Tex. Civ. App. 94, 27 S. W. 803; Steger v. Davis, 8 Tex. Civ. App. 23, 27 S. W. 1068; Wright v. Pipe Line Co., 101 Pa. St. 204; Seymour v. Society, 54 Minn. 147, 55 N. W. 907; Magee v. Improvement Co., 98 Cal. 678, 33 Pac. 772; Manchester & L. R. Co. v. Concord R. Co., 66 N. H. 100, 20 Atl. 383; Union Hardware Co. v. Plume & Atwood Manuf'g Co., 58 Conn. 219, 20 Atl. 455.

contract, the other party may maintain an action on the contract itself for the price agreed upon.⁵³ So it has been held that, if the price has been paid under an ultra vires contract for the purchase of goods, an action may be maintained on the contract for failure to deliver the goods. And if a corporation sells and delivers goods in carrying on a business that is merely ultra vires, it has been held that the purchaser cannot defeat an action for the price on the ground that the sale was ultra vires.⁵⁴ So, if a corporation borrows money for an unauthorized purpose, and gives its note or other obligation therefor, it cannot set up the ultra vires character of the contract to defeat an action thereon.⁵⁵ And the same rule applies where a corporation lends money or furnishes other consideration under an ultra vires contract, and takes the other party's note therefor. The other party cannot set up the ultra vires character of the contract to defeat an action by the corporation.⁵⁶

On the same principle it has been held that if a corporation engages in the business of an innkeeper, it cannot escape an innkeeper's liability to a guest, as for property lost, by setting up that the business was not authorized by its charter.⁵⁷ So where a street-railway company agreed to pay a certain sum if the state board of agriculture would hold the state fair at a certain place, it was held that the company could not set up the defense of ultra vires to defeat liability on its contract, after the fair was held at the place agreed upon, and it had the benefit therefrom in its increased traffic.⁵⁸ So where a fire insurance company which had issued a policy of insurance

⁵³ *Wright v. Pipe Line Co.*, 101 Pa. St. 204; *Dewey v. Railroad Co.*, 91 Mich. 351, 51 N. W. 1063; *Towers Excelsior & Ginnery Co. v. Inman*, 96 Ga. 506, 23 S. E. 418; and other cases in note 52, *supra*.

⁵⁴ *Slater Woolen Co. v. Lamb*, 143 Mass. 420, 9 N. E. 823, 1 Cumming, Cas. Priv. Corp. 260.

⁵⁵ *Bradley v. Ballard*, 55 Ill. 413, 1 Cumming, Cas. Priv. Corp. 249, W. D. Smith, Cas. Corp. 137, Shep. Cas. Corp. 68.

⁵⁶ *Steam Nav. Co. v. Weed*, 17 Barb. (N. Y.) 378, 2 Cumming, Cas. Priv. Corp. 55; *Logan v. Association*, 8 Tex. Civ. App. 490, 28 S. W. 141; *Gorrell v. Insurance Co.*, 11 O. C. A. 240, 63 Fed. 371; *Pooch v. Association*, 71 Ind. 357; *Pan-coast v. Insurance Co.*, 79 Ind. 172.

⁵⁷ *Magee v. Improvement Co.*, 98 Cal. 678, 33 Pac. 772.

⁵⁸ *State Board of Agriculture v. Citizens' St. Ry. Co.*, 47 Ind. 407, 1 Cumming, Cas. Priv. Corp. 222.

against loss of crops caused by hail, and received the premium, sought to escape liability for a loss on the ground that it had no power to insure against loss by hail, the court held that the defense should not be allowed.⁵⁹

Same—Action Maintainable by the Corporation.

According to this doctrine, as shown by the illustrations referred to in the preceding paragraph, the right of action is not limited to the other party to the contract, but the corporation may maintain an action where it has performed its part of the contract. [“It is very well settled,” said the New York court in a leading case, “that a corporation cannot avail itself of the defense of ultra vires when the contract has been, in good faith, fully performed by the other party, and the corporation has had the full benefit of the performance and of the contract.”] * * * The same rule holds e converso. If the other party has had the benefit of a contract fully performed by the corporation, he will not be heard to object that the contract and performance were not within the legitimate powers of the corporation.”⁶⁰

Same—The Ground of This Doctrine.

The true ground of this doctrine is that of equitable estoppel, whereby the defendant is not permitted to rely upon or show the invalidity of the contract. “In such a case the contract is assumed by the court to be valid, the party seeking to avoid it not being permitted to attack its character in this respect.”⁶¹ The reasons by which the courts have been influenced are obvious. It was said by Chief Justice Comstock: Commercial manufacturing, and trading corporations “are brought into relation with almost every member of the community, and I think it greatly to be desired that in laying down the rules of law which are to govern in such relations, we should avoid a system of destructive technicalities. Those rules should be founded in the principles of justice which are recognized

⁵⁹ Denver Fire Ins. Co. v. McClelland, 9 Colo. 11, 9 Pac. 771, 1 Cumming, Cas. Priv. Corp. 227.

⁶⁰ Whitney Arms Co. v. Barlow, 63 N. Y. 62, 1 Cumming, Cas. Priv. Corp. 263.

⁶¹ Denver Fire Ins. Co. v. McClelland, 9 Colo. 11, 9 Pac. 771, 1 Cumming, Cas. Priv. Corp. 227.

in other and analogous dealings among men.”⁶² It would be carrying the doctrine concerning ultra vires contracts to an unwarranted extent, said the Indiana court, “to hold that a corporation might obtain the money of another, and, with the fruits of the contract in its treasury, interpose the defense of ultra vires; or, having used the money with the consent or acquiescence of its stockholders, ask that the lender be restrained from collecting it back, on the ground that the money was obtained in violation of the charter of the corporation. Like natural persons, corporations must be held to the observance of the recognized principles of common honesty and good faith, and these principles render the doctrine of ultra vires unavailing when its application would accomplish an unjust end, or result in the perpetration of a legal fraud. After a corporation has received the fruits which grow out of the performance of an act ultra vires, and the mischief has all been accomplished, it comes with an ill grace then to assert its want of power to do the act or make the contract, in order to escape the performance of an obligation it has assumed. The most that can be said in the present case is that there was a defect of power to engage in the transaction in which the money borrowed was used. The power to borrow money was plenary, and subject to no restrictions. In such a case, although the lender may know that it is the purpose of the borrower to use the money in an irregular way, yet, if the contract between the lender and borrower is not in violation of law, or declared void by statute, the money may be recovered, unless the lender was in some way implicated in furthering the borrower’s design or accessory to the prohibited or illegal act.”⁶³

Same—Necessity for Performance by the Plaintiff.

The courts which hold this doctrine require that there shall have been some performance on the part of the plaintiff which will render

⁶² Per Comstock, C. J., in *Bissell v. Railroad Co.*, 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 187, 190.

⁶³ *Wright v. Hughes*, 119 Ind. 324, 21 N. E. 907. “The rule requiring the observance of good faith and fair dealing is as applicable to corporations as to individuals. Neither can involve others in onerous engagements, and with the consideration of the contract in their possession, disavow their acts, to the damage and discomfiture of others, unless it clearly appears that there was an absolute want of capacity to make the contract.” *Louisville, N. A. & C. Ry. Co. v. Flanagan*, 113 Ind. 488, 14 N. E. 370.

it unjust and inequitable to permit the defendant to set up the ultra vires character of the contract in defense. They will not lend their aid to enforce an ultra vires contract that is wholly executory.⁶⁴ And the fact that the contract has been partly performed on one or both sides does not always require enforcement as to the residue. It will not be enforced unless its enforcement is necessary to do justice. Thus, where a corporation empowered to purchase material for manufacturing purposes purchased a quantity of material for the purpose of selling it again on speculation, the seller knowing of its purpose, it was held that the contract was void; that either party could repudiate it after part performance by both parties, and on repudiation of it by the seller, and in a suit by him to recover the value of the material already delivered, the corporation could not recover damages for his failure to perform the residue.⁶⁵ +

Same—Answers to Arguments against This Doctrine.

One of the arguments used in support of the doctrine that no action can be maintained against a corporation on an ultra vires contract is that one dealing with a corporation is bound to know the extent of its powers to contract; that the act under which it exists, and the record of its charter or articles of association, furnish notice of the extent and limitation of its corporate powers and authority to contract. In answer to this it was said by the supreme court of Colorado: "While, as a general proposition, this is true, yet it must be conceded that this constructive notice is of a very vague and shadowy character. Every one may have access to the statutes of the states affecting companies incorporated thereunder, and to their articles of incorporation; but to impute a knowledge of the probable construction the courts would put upon these statutes and articles of incorporation to determine questions raised upon a given contract proposed is carrying the doctrine of notice to an extent which can only be denominated preposterous."⁶⁶ And Chief Jus-

⁶⁴ *Nassau Bank v. Jones*, 95 N. Y. 115, 1 Cumming, Cas. Priv. Corp. 293; *Bradley v. Ballard*, 55 Ill. 413; *Bosshardt & Wilson Co. v. Crescent Oil Co.*, 171 Pa. St. 109, 32 Atl. 1120.

⁶⁵ *Day v. Buggy Co.*, 57 Mich. 151, 23 N. W. 628, 1 Cumming, Cas. Priv. Corp. 261.

⁶⁶ *Denver Fire Ins. Co. v. McClelland*, 9 Colo. 11, 9 Pac. 771, 1 Cumming, Cas. Priv. Corp. 227.

tice Comstock observed in a New York case that "a traveler from New York to Mississippi could hardly be required to furnish himself with the charters of all the railroads on his route, or to study a treatise on the law of corporations," in order to satisfy himself that the railroad companies are not operating their roads in an ultra vires manner.⁶⁷

Another argument in support of the doctrine that an action should not be allowed on an ultra vires contract is that public policy and the interests of the state require that corporations shall be kept within the legitimate exercise of their powers. In answer to this it has been said: "This may be true to a certain extent, and the state may interpose to revoke their charters for an abuse thereof; but we take it that it is no more the public policy of the state to protect the business of private corporations than that of its individual citizens; and to invoke public policy in a case like the one at bar [a case in which a corporation pleaded ultra vires in an action against it on a contract fully performed by the other party by payment of the consideration], in order to prevent a corporation from doing wrong, by punishing the other party, would differ little from asking a court, on the ground of public policy, to prevent the obtaining of money or goods through false pretenses by holding that the party defrauded should be punished by the loss of his money or goods."⁶⁸

It has also been said that the interests of the stockholders require that corporations be held strictly within their legitimate powers, so that the capital shall not be subjected to the risk of enterprises not contemplated by the charter, and therefore not authorized by the stockholders in subscribing for the stock. In answer to this argument, it is sufficient to say that the stockholders control or influence the corporation, and are acting as a corporation for their personal benefit, while persons dealing with it have no control or influence over it, nor interest in it. There is no reason, therefore, why the stockholders should be protected at the expense of the public.

⁶⁷ Per Comstock, C. J., in *Bissell v. Railroad Co.*, 22 N. Y. 259, 1 Cumming, Cas. Priv. Corp. 187.

⁶⁸ *Denver Fire Ins. Co. v. McClelland*, 9 Colo. 11, 9 Pac. 771, 1 Cumming, Cas. Priv. Corp. 227.

Same—Specific Performance.

It has been held that a court of equity will not compel specific performance of an ultra vires contract, even though it may have been partly performed by the complainant. In a Michigan case, a bank had entered into an ultra vires contract to purchase land from a third person, and sell it to the defendant. After the land had been purchased by the bank, the defendant refused to carry out the contract, and the bank brought suit in equity for specific performance. The court held that the relief could not be granted, as it could not, consistently with equitable principles, assist the bank to carry into execution a contract to violate its charter, and that the purchase of the property by the bank after the contract was made could make no difference. "Equity," it was said, "will aid no one in doing that which is unlawful." ⁶⁹

ILLEGAL CONTRACTS.

68. Contracts of a corporation may be illegal on other grounds than because they are ultra vires; that is, unlawful in the sense in which a contract by an individual may be unlawful. A contract which is illegal in this sense is subject to the same rules that govern illegal contracts by individuals. Generally, no action can grow out of it.

Contracts of corporations may not only be ultra vires, but, like the contracts of an individual, they may, on other grounds, be illegal in the sense of the maxim, "Ex turpi causa non oritur actio." In the absence of express statutory provision to the contrary, a corporation can make no contract which would be illegal if it were made by an individual. Thus a contract by a corporation, like a contract by an individual, is illegal if it contemplates the publication of a libel, or a fraud upon third persons, or the doing of an act which is prohibited by statute under a penalty, or if it is contrary to public policy, as in the case of wagering contracts, contracts in restraint of trade, etc. A corporation authorized by its charter to engage in the

⁶⁹ *Bank of Michigan v. Niles*, Walk. (Mich.) 99, 1 Doug. 401, 1 Cumming, Cas. Priv. Corp. 291.

business of manufacturing and selling an article or product, and to own the property necessary for that purpose, has no right to buy up the business and property of all the other persons and companies engaged in the business, for the purpose of obtaining a monopoly; and, if it does so, quo warranto proceedings may be maintained by the state to oust it from the exercise of its franchise.⁷⁰ The principles of law which apply to illegal contracts are substantially the same where the contract is by a corporation as where it is by an individual. The student, therefore, must refer in this connection to works on the general law of contracts.⁷¹ There are a few questions that are peculiar to corporations.

Even in those jurisdictions where the ultra vires contracts of a corporation are not regarded as illegal in the sense that no action can be maintained upon them, unless there is an express prohibition in the charter or in some statute, there are some exceptions. An ultra vires contract that is not expressly prohibited will nevertheless be declared illegal if it is in its nature and effect clearly contrary to public policy. Thus it has been held in New York that a contract by which a bank, organized under the laws of the state, subscribes for or agrees to purchase stock in a railroad company, and so to be a stockholder therein, and subject to liability as such, is not merely ultra vires, but is illegal, though not expressly prohibited. "The spirit of the law," it was said, "as well as a sound public policy, forbid these institutions from risking the moneys intrusted to their care in doubtful speculations or enterprises."⁷²

Contracts Disabling Corporations from Performing Duties to the Public.

A railroad, steamboat, gas, water, or other like corporation can make no contract which will interfere with its performance of the duties which it owes to the public. Such a contract is not merely ultra vires. It is illegal, and absolutely void, as being contrary to public policy. It is a well-settled principle "that where a corporation, like a railroad company, has granted to it by charter a franchise intended in large measure to be exercised for the public good, the due

⁷⁰ *Distilling & Cattle Feeding Co. v. People*, 156 Ill. 448, 41 N. E. 188; post, p. 240.

⁷¹ See Clark, *Cont.* 374-507.

⁷² *Nassau Bank v. Jones*, 95 N. Y. 115, 1 Cumming, *Cas. Priv. Corp.* 293.

performance of those functions being the consideration of the public grant, any contract which disables the corporation from performing those functions, which undertakes, without the consent of the state, to transfer to others the rights and powers conferred by the charter, and to relieve the grantees of the burden which it imposes, is a violation of the contract with the state, and is void as against public policy."⁷³

Effect of Express Prohibition in Charter.

If the charter of a corporation, instead of merely not authorizing a certain contract, expressly prohibits it, the contract stands upon a different footing from one that is merely ultra vires. As a rule, it is illegal and void, and no action can be maintained upon it, or grow out of it. The maxim, "Ex turpi causa non oritur actio," applies.⁷⁴ In *White v. Franklin Bank*⁷⁵ the defendant had taken a deposit for a certain time, and promised to repay it at the expiration of that time, in violation of a statute declaring that no bank should make or issue any note, bill, check, draft, acceptance, certificate, or contract, in any form whatever, for the payment of money, at any future day certain, etc. It was held that the transaction was illegal and void, because expressly prohibited by statute, and that no action could be maintained on the contract.

If the charter of a corporation, including statutes applicable to it, merely prohibits certain contracts, and does not declare that contracts in violation of the prohibition shall be void, and the purpose

⁷³ *Thomas v. Railroad Co.*, 101 U. S. 71, 1 Cumming, Cas. Priv. Corp. 164, W. D. Smith, Cas. Corp. 132, Shep. Cas. Corp. 70. And see *York & M. L. R. Co. v. Winans*, 17 How. 30; *American Union Tel. Co. v. Union Pac. Ry. Co.*, 1 McCrary, 188, 1 Fed. 745, 1 Cumming, Cas. Priv. Corp. 284; *Black v. Canal Co.*, 22 N. J. Eq. 390. In *Thomas v. Railroad Co.*, supra, one railroad company had leased its road to another, and the transaction was held illegal as against public policy. In *American Union Tel. Co. v. Union Pac. Ry. Co.*, supra, a railroad company, authorized to also construct and operate a telegraph line, leased the telegraph line to another corporation, and the lease was held illegal and void. In *Visalia Gas & Electric Light Co. v. Sims*, 104 Cal. 326, 37 Pac. 1042, a contract by which a corporation organized to operate gas and electric light works leased them to another was held ultra vires, and void as against public policy.

⁷⁴ *Leavitt v. Palmer*, 3 N. Y. 19; *White v. Bank*, 22 Pick. (Mass.) 181, 1 Cumming, Cas. Priv. Corp. 239.

⁷⁵ 22 Pick. (Mass.) 181, 1 Cumming, Cas. Priv. Corp. 239.

of the statute does not show an intention on the part of the legislature to make such contracts void, they are binding; and objection on the ground that they were prohibited can only be raised by the state in a direct proceeding against the corporation to forfeit its charter.⁷⁶ The national banking act impliedly prohibits national banks from lending money on real estate. In *National Bank v. Matthews*⁷⁷ a loan was made by a national bank on a note secured by a deed of trust on real estate, and a maker of the note and grantor in the deed filed a bill in equity to enjoin a sale under the deed to satisfy the note. The supreme court of the United States, assuming the transaction to be within the prohibition, held that the statute, in prohibiting such a contract, did not make it void, and that the state only could object to the excess of power in a proceeding to forfeit the bank's charter. "We cannot believe," said the court, "it was meant that stockholders, and perhaps depositors and other creditors, should be punished and the borrower rewarded, by giving success to this defense whenever the offensive fact should occur. The impending danger of a judgment of ouster and dissolution was, we think, the check, and none other, contemplated by congress. This has been always the punishment prescribed for the wanton violation of a charter, and it may be made to follow whenever the proper public authority shall see fit to invoke its application. A private person cannot, directly or indirectly, usurp this function of the government."⁷⁸ So where a bank charter prohibited directors or other officers of the bank from borrowing money from the bank under penalty of fine and imprisonment, and an officer borrowed money from the bank in violation thereof, it was held that the claim of the bank to recover the loan was enforceable.⁷⁹

Effect of Illegality—Actions in Disaffirmance of Illegal Contract.

It is a well-settled doctrine of the law of contracts, that where money has been paid by one party to another under a contract that is

⁷⁶ *National Bank v. Matthews*, 98 U. S. 621, 1 Cumming, Cas. Priv. Corp. 95; *National Bank v. Whitney*, 103 U. S. 99, 1 Cumming, Cas. Priv. Corp. 102; *Silver Lake Bank v. North*, 4 Johns. Ch. (N. Y.) 370.

⁷⁷ 98 U. S. 621, 1 Cumming, Cas. Priv. Corp. 95.

⁷⁸ Mr. Justice Miller dissented, holding that it was the intention of congress to make such contracts void. The case was adhered to and followed in *National Bank v. Whitney*, supra.

⁷⁹ *Lester v. Bank*, 33 Md. 558.

illegal as involving moral turpitude, both parties being *particeps criminis*, no action can be maintained to recover it back. The same is true generally where the contract is illegal because prohibited by statute, or because contrary to public policy. The rules of law governing these cases may be thus stated:

In no case can an action be sustained to enforce the illegal agreement itself.⁸⁰ And, as a general rule, where an illegal agreement has been executed in whole or in part by the payment of money, or the transfer of property, or rendition of services, the court will not lend its aid to enable the party, even in disaffirmance of the contract, to recover back the money, or to recover the value of the goods or services.⁸¹ The latter rule is subject to some exceptions.⁸²

In some cases, where the contract is merely *malum prohibitum*, a *locus poenitentiae* remains, and while the prohibited promise is unperformed money or goods delivered in consideration of it may be recovered. This exception is not at all peculiar to contracts of corporations.⁸³

Again, where the contract is only illegal because prohibited by statute, and the parties are not in *pari delicto*, the one who is less guilty may disaffirm the contract, and recover what he has parted with. Such is the case where the party asking relief was induced to enter into the contract under the influence of fraud or duress.⁸⁴ So it is, also, where the statutory prohibition was intended for the pro-

⁸⁰ Clark, Cont. 491.

⁸¹ Clark, Cont. 491.

⁸² In New York it is held that where a corporation discounts commercial paper without authority it may recover the money loaned, though the securities are void. "It is no doubt the general rule of law," said the court in such a case, "that no right of action can spring out of an illegal contract. And the rule that an illegal contract cannot be enforced applies as well to contracts *malum prohibitum* as to contracts *malum in se*. But it does not necessarily follow that all the consequences attending a contract which is contrary to public morals, or founded on an immoral consideration, attend and affect a contract *malum prohibitum* merely. The law in the former case will not undertake to relieve the parties from the position in which they have placed themselves, or to adjust the equities between them. But in the latter case, while the law will not enforce the prohibited contract, it will take notice of the circumstances, and, if justice and equity require a restoration of money or property received by either party thereunder, it will, and in many cases has, given relief." *Pratt v. Short*, 79 N. Y. 437.

⁸³ Clark, Cont. 494.

⁸⁴ Clark, Cont. 498.

tection of the party asking relief.⁸⁵ As illustrating this principle may be mentioned cases in which banks or other corporations are prohibited from issuing notes, bills, or other securities. It is held by some courts in these and similar cases that the prohibition is intended to protect the public against the prohibited securities, that the corporation is the only offender, and that the persons who receive them may recover the money paid for them, not being in *pari delicto*. "The corporation issuing the bills contrary to law and against penal sanction is deemed more guilty than the members of the community who receive them, whenever the receiving of them is not expressly prohibited. The latter are regarded as the persons intended to be protected by the law; and if they have not themselves violated an express law in receiving the bills, the principles of justice require that they should be able to recover the money received by the bank for them."⁸⁶

Most courts hold that where the direct object of a contract is innocent in itself, but the intention of one of the parties is unlawful,—as where goods are bought or money borrowed to be used for an unlawful purpose, which is not *malum in se*,—the fact that the other party knows of the unlawful purpose does not render the agreement illegal, so as to prevent his maintaining an action thereon, unless it is made part of the contract that the money or goods shall be used for such purpose, or unless he has done something in aid or furtherance of the unlawful design beyond merely entering into the contract.⁸⁷ And this principle has been applied to contracts with a corporation, where the corporation intended to use the money or goods obtained by it under the contract for an illegal purpose.⁸⁸

⁸⁵ Clark, Cont. 500; Thomas v. City of Richmond, 12 Wall. 849; White v. Bank, 22 Pick. (Mass.) 181; 1 Cumming, Cas. Priv. Corp. 239; Tracy v. Talmage, 14 N. Y. 162, 2 Cumming, Cas. Priv. Corp. 67; Oneida Bank v. Ontario Bank, 21 N. Y. 490.

⁸⁶ Thomas v. City of Richmond, *supra*.

⁸⁷ Clark, Cont. 478–486, where the cases are collected, and the conflict in the decisions of the different states is pointed out.

⁸⁸ Tracy v. Talmage, 14 N. Y. 162, 2 Cumming, Cas. Priv. Corp. 67. And see Curtis v. Leavitt, 15 N. Y. 1.

CHAPTER VII.

POWERS AND LIABILITIES OF CORPORATIONS (Continued).

69. Liability for Torts.

70-72. Responsibility for Crime—Contempt of Court.

LIABILITY FOR TORTS.

69. A private corporation is liable for the torts of its servants and agents committed in the course of their employment, to the same extent as a natural person would be. And it may be liable for wrongs involving a mental element, as malicious wrongs, fraud, etc. But it cannot commit a tort, like slander, which, from its nature, cannot be committed by deputy.

At one time it was doubted whether a corporation could be sued for a tort, but it is now settled that for most torts it may be liable to the same extent as a natural person would be under the same circumstances. It is said that a corporation has no power to do an act not authorized by its charter, and, as we have seen, this is true in a sense; but it is not meant by this that it cannot do wrong.¹ The word "power" is used in the sense of "authority." A corporation has no right to exceed the powers conferred upon it, but it has the capacity to do so; and if, in doing so, it commits a tort, it is as fully liable as a natural person would be under similar circumstances.² "Corporations are liable for every wrong of which they are

¹ Ante, p. 164; post, p. 197.

² Chestnut Hill & S. H. Turnpike Co. v. Rutter, 4 Serg. & R. (Pa.) 6, 1 Cumming, Cas. Priv. Corp. 431; Goodspeed v. Bank, 22 Conn. 530, 1 Cumming, Cas. Priv. Corp. 443; New York, L. E. & W. R. Co. v. Haring, 47 N. J. Law, 137, 2 Cumming, Cas. Priv. Corp. 110; Philadelphia, W. & B. R. Co. v. Quigley, 21 How. 202, 1 Cumming, Cas. Priv. Corp. 453, Shep. Cas. Corp. 144; Yarborough v. Bank, 16 East, 6, 1 Cumming, Cas. Corp. 428; Hutchinson v. Railroad Co., 6 Heisk. (Tenn.) 634, 2 Cumming, Cas. Priv. Corp. 102; Maund v. Canal Co., 4 Man. & G. 452, 1 Cumming, Cas. Priv. Corp. 429; Central Railroad & Banking
Olk.Pr.Corp.—13

guilty, and in such cases the doctrine of ultra vires has no application.”³ The maintenance of a ferry by an educational corporation is ultra vires. The corporation is nevertheless liable for injuries to a passenger being transported thereon for hire, caused by the negligence of the employé in charge.⁴ As we shall see in a subsequent chapter, some courts do not hold a corporation liable for torts of employés in ultra vires transactions.⁵

A corporation, being impersonal, cannot personally commit a tort. It can act only through an agent, and it can, therefore, commit no tortious act that cannot be committed by a natural person by deputy. For such wrongful acts as can only be committed by the wrongdoer directly, it cannot be liable.⁶ A natural person cannot commit slander by deputy, nor can a corporation commit slander.⁷ On the other hand, it is well settled that for any tort which can be committed by an agent corporations may be liable. “Wherever they can competently do or order any act to be done on their behalf, * * * they are liable to the consequences of such act, if it be of a tortious nature, and to the prejudice of others.”⁸ Thus a corporation may be liable in trover for the conversion of goods;⁹ in trespass quare clausum fregit;¹⁰ in trespass de bonis asportatis;¹¹ in trespass for assault and battery, false imprisonment, etc.;¹² in case for obstruct-

Co. v. Smith, 76 Ala. 572, 52 Am. Rep. 353; Eastern Counties Ry. Co. v. Broom, 6 Exch. 314, 1 Cumming, Cas. Priv. Corp. 434; Green v. Omnibus Co., 7 C. B. (N. S.) 290, 1 Cumming, Cas. Priv. Corp. 440; Nims v. Mt. Hermon Boys' School, 160 Mass. 177, 35 N. E. 776; Mersey Docks & Harbour Board Trustees v. Gibbs, L. R. 1 H. L. 93.

³ Merchants' Bank v. State Bank, 10 Wall. 604. But see Gunn v. Railroad Co., 74 Ga. 509, 2 Cumming, Cas. Priv. Corp. 111.

⁴ Nims v. Mt. Hermon Boys' School, 160 Mass. 177, 35 N. E. 776.

⁵ Post, p. 523.

⁶ 1 Jagg. Torts, 170.

⁷ 1 Jagg. Torts, 170; Townsh. Sland. & L. § 265.

⁸ Yarborough v. Bank, 16 East, 6, 1 Cumming, Cas. Priv. Corp. 426.

⁹ Yarborough v. Bank, supra; Beach v. Bank, 7 Cow. (N. Y.) 485. Trespass for mesne profits. M'Cready v. Guardians of the Poor, 9 Serg. & R. (Pa.) 94.

¹⁰ Maund v. Canal Co., 4 Man. & G. 452, 1 Cumming, Cas. Priv. Corp. 429.

¹¹ Maund v. Canal Co., supra.

¹² Eastern Counties Ry. Co. v. Broom, 6 Exch. 314, 1 Cumming, Cas. Priv. Corp. 434; New York, L. E. & W. R. Co. v. Haring, 47 N. J. Law, 137, 2 Cumming, Cas. Priv. Corp. 110; Wheeler & W. Manuf'g Co. v. Boyce, 36 Kan. 350,

ing, diverting, or polluting a water course;¹³ and for nuisances generally.¹⁴

Liability in tort will also attach to a corporation for the negligence of its servants or agents in omitting to perform a duty resting upon the corporation.¹⁵ And it may be liable for negligence in the performance of acts by its servants or agents. Thus it may be liable for negligence in the custody or use of a vicious dog, or other animate instrumentality, or of powder, poison, or other inanimate instrumentality. A railroad company is liable in tort for negligence in the running or management of its trains, or for keeping its premises in an unsafe condition. And any other private corporation which keeps its premises in an unsafe condition will be liable for injuries caused thereby.¹⁶

It has been contended that, since a corporation is merely an artificial being, without mind or soul, it cannot commit a tort involving a mental operation, and that it cannot, therefore, be liable for malicious wrongs, or wrongs involving a specific intent, such as libel, malicious prosecution, or fraud.¹⁷ It is now well settled, however, that the mental attitude of its agents, like their acts, may be imputed to a corporation, and that a corporation may be guilty of malice in contemplation of law.¹⁸ Corporations, therefore, have been held liable for a libel published by their agents;¹⁹ for a mali-

13 Pac. 609; *Moore v. Railroad Corp.*, 4 Gray (Mass.) 465; *Krulevitz v. Railroad Co.*, 140 Mass. 573, 5 N. E. 500; *Denver & R. G. Ry. Co. v. Harris*, 122 U. S. 597, 7 Sup. Ct. 1286; *Id.*, 3 N. M. 109, 2 Pac. 369.

13 *Chestnut Hill & S. H. Turnpike Co. v. Rutter*, 4 Serg. & R. (Pa.) 6, 1 Cumming, Cas. Priv. Corp. 431.

14 *Baltimore & P. R. Co. v. Fifth Baptist Church*, 108 U. S. 317, 2 Sup. Ct. 719.

15 *Nims v. Mt. Hermon Boys' School*, 160 Mass. 177, 35 N. E. 776; *Riddle v. Proprietors of the Locks, etc.*, 7 Mass. 169; *Mersey Docks & Harbour Board Trustees v. Gibbs*, L. R. 1 H. L. 93; *Hutchinson v. Railroad Co.*, 6 Heisk. (Tenn.) 634, 2 Cumming, Cas. Priv. Corp. 102; *Townsend v. Turnpike Road*, 6 Johns. (N. Y.) 90; *Hooker v. New Haven & N. Co.*, 14 Conn. 146.

16 See cases cited above.

17 *Childs v. Bank*, 17 Mo. 213.

18 1 Jagg. Torts, 168; *Green v. Omnibus Co.*, 7 O. B. (N. S.) 290, 1 Cumming, Cas. Priv. Corp. 440; *Goodspeed v. Bank*, 22 Conn. 530, 1 Cumming, Cas. Priv. Corp. 443; *Merrills v. Manufacturing Co.*, 10 Conn. 384. See *Lake Shore & M. S. Ry. Co. v. Prentice*, 147 U. S. 101, 13 Sup. Ct. 291, *Shep. Cas. Corp.* 153.

19 *Philadelphia, W. & B. R. Co. v. Quigley*, 21 How. 202, 1 Cumming, Cas.

cious criminal prosecution;²⁰ for a malicious and vexatious attachment;²¹ and for conspiracy;²² and corporations have repeatedly been held liable for false representations made by their agents. The rule is well settled that, in cases of fraud, a corporation will be liable whenever an individual would be held liable.²³

In *Green v. London General Omnibus Co.*,²⁴—a leading English case,—the plaintiff was the proprietor of an omnibus line, engaged in the carriage of passengers, and the defendant was a corporation, and the proprietor of a rival line. The declaration sought to recover damages for acts alleged to have been wrongfully and maliciously done by the defendant for the purpose of obstructing, and which did obstruct, the plaintiff in his business; such as the intentional driving of the defendant's vehicles against those of the plaintiff. The defendant demurred on the ground that a corporation could not be guilty of a willful and intentional wrong; but the court held that the declaration was good. In *Goodspeed v. East Haddam Bank*,²⁵—a leading case in this country,—the action was brought against a bank for maliciously prosecuting a vexatious suit, and it was held that the action could be maintained.²⁶

Priv. Corp. 453, *Shep. Cas. Corp.* 144; *Bacon v. Railroad Co.*, 55 Mich. 224, 21 N. W. 324.

²⁰ *Turner v. Insurance Co.*, 55 Mich. 236, 21 N. W. 326; *Krulevitz v. Railroad Co.*, 140 Mass. 573, 5 N. E. 500; *Reed v. Bank*, 130 Mass. 445; *Copley v. Machine Co.*, 2 Woods, 494, Fed. Cas. No. 3,213.

²¹ *Goodspeed v. Bank*, 22 Conn. 530, 1 Cumming, Cas. Priv. Corp. 443; *Western News Co. v. Wilmarth*, 33 Kan. 510, 6 Pac. 786.

²² *Buffalo Lubricating Oil Co. v. Standard Oil Co.*, 106 N. Y. 669, 12 N. E. 826.

²³ *Barwick v. Bank*, L. R. 2 Exch. 259; *Nevada Bank of San Francisco v. Portland Nat. Bank*, 59 Fed. 338; *Cragie v. Hadley*, 99 N. Y. 131, 1 N. E. 537; *Fifth Ave. Bank of New York v. Forty-Second St. & G. St. Ferry R. Co.*, 137 N. Y. 231, 33 N. E. 878; *Shaw v. Mining Co.*, 13 Q. B. Div. 103; *Tome v. Railroad Co.*, 39 Md. 36.

²⁴ 7 C. B. (N. S.) 290; 1 Cumming, Cas. Priv. Corp. 440.

²⁵ 22 Conn. 530, 1 Cumming, Cas. Priv. Corp. 443.

²⁶ It was said by Church, C. J., in this case: "The claim is that, as a corporation is ideal only, it cannot act from malice, and therefore cannot commence and prosecute a malicious or vexatious suit. This syllogism or reasoning might have been very satisfactory to the school men of former days; more so, we think, than to the jurist who seeks to discover a reasonable and appropriate remedy for every wrong. To say that a corporation cannot have motives, and act from mo-

A corporation may not only be held liable for the actual damages resulting from a malicious wrong, but it may also, by the weight of authority, be held liable for exemplary damages, where, under similar circumstances, a natural person would be held so liable.²⁷

Authority of Servant or Agent.

A corporation is liable for the acts of its servants and agents, including their wrongful acts, on the same principles, and to the same extent only, as a natural person is liable for the acts of his servant or agent. If a corporation expressly authorizes its servant or agent to do a particular act, there can be no question as to its liability. Thus, if a majority of the stockholders should by vote direct an agent to enter unlawfully upon the land of another, the corporation would clearly be liable in trespass. Difficulties arise in those cases where the authority of the agent is to be implied. It is the general rule that a corporation, like a natural person, is liable for any act of its servant or agent that is committed in the conduct of its business, and in the course of his employment. This rule will be considered in treating of the liability of a corporation for the acts of its agents.²⁸

RESPONSIBILITY FOR CRIME—CONTEMPT OF COURT.

70. A corporation may be criminally responsible for omission to perform a duty imposed upon it by law, or for nonfeasance.

tives, is to deny the evidence of our senses, when we see them thus acting, and effecting thereby results of the greatest importance every day. And if they can have any motive, they can have a bad one; they can intend to do evil, as well as to do good. If the act done is a corporate one, so must the motive and intention be. In the present case, to say that the vexatious suit, as it is called, was instituted, prosecuted, and subsequently sanctioned by the bank in the usual modes of its action, and still to claim that, although the acts were those of the bank, the intention was only that of the individual directors, is a distinction too refined, we think, for practical application."

²⁷ *Wheeler & Wilson Manuf'g Co. v. Boyce*, 36 Kan. 350, 13 Pac. 609; *Denver & R. G. Ry. Co. v. Harris*, 122 U. S. 597, 7 Sup. Ct. 1286; *Merrills v. Manufacturing Co.*, 10 Conn. 384. Compare *Lake Shore & M. S. Ry. Co. v. Prentice*, 147 U. S. 101, 13 Sup. Ct. 261, *Shep. Cas. Corp.* 153.

²⁸ *Post*, p. 523.

- 71. In most states, but not in all, it is held that it may be criminally responsible for some acts of misfeasance, such as maintaining a nuisance. But it cannot commit a crime which involves a mental operation, nor crimes involving an element of personal violence.**
- 72. A corporation may be punished for contempt of court.**

Nonfeasance.

Though there is dictum in some of the old cases to the contrary, it is now perfectly well settled that a corporation may be indicted for omission to perform a duty to the public imposed upon it by law, and, though it cannot be imprisoned, it may be fined, and deprived of its charter.²⁹ Thus a railroad company may be indicted and fined for failure to comply with a statute requiring it to keep a bridge in repair across a cut where its road crosses a public highway.³⁰

Misfeasance.

It has been held that a corporation cannot be indicted for misfeasance,—that it “can neither commit a crime or misdemeanor by any positive or affirmative act, nor incite others to do so.”³¹ Thus, in the case from which this quotation is taken, it was held in Maine that a corporation could not be indicted for maintaining a nuisance by obstructing a navigable river, though the obstruction was directed by a majority of the stockholders; but that the indictment should have been against the individuals.³²

The great weight of modern authority, however, is against this position, and to the effect that an indictment will lie against a corporation for misfeasance as well as for nonfeasance,³³ provided the

²⁹ Clark, Cr. Law, 78-80; Reg. v. Railway Co., 3 Q. B. 223; New York & G. L. R. Co. v. State, 50 N. J. Law, 303, 13 Atl. 1, affirmed 53 N. J. Law, 244, 23 Atl. 168. In Anon., 12 Mod. 559, Case 935, it was said that “a corporation is not indictable, but the particular members of it are.” But it does not appear what the indictment was for.

³⁰ New York & G. L. R. Co. v. State, *supra*.

³¹ State v. Great Works Milling & Manufacturing Co., 20 Me. 41; Com. v. President, etc., of Swift Run Gap Turnpike Co., 2 Va. Cas. 362; State v. Ohio & M. R. Co., 23 Ind. 362 (since changed by statute in Indiana. See State v. Baltimore, O. & C. R. Co., 120 Ind. 298, 22 N. E. 307).

³² State v. Great Works Milling & Manufacturing Co., *supra*.

³³ Clark, Cr. Law, 79; Reg. v. Great North of England Ry. Co., 2 Cox, Cr.

offense involves no mental element, nor element of personal violence. Thus corporations have repeatedly been held liable for nuisance by obstructing a navigable river, or other public highway.³⁴ And an indictment has been sustained against a corporation for nuisance in keeping a disorderly house,³⁵ and for permitting gaming on its premises.³⁶ "Corporations" said the Massachusetts court, "cannot be indicted for offenses which derive their criminality from evil intention, or which consist in a violation of those social duties which appertain to men and subjects. They cannot be guilty of treason or felony, of perjury, or offenses against the person. But beyond this there is no good reason for their exemption from the consequences of unlawful and wrongful acts committed by their agents in pursuance of authority derived from them."³⁷

Offenses Involving Mental Element or Personal Violence.

We have seen that a corporation may be held liable in tort for malicious wrongs, such as libel and malicious prosecution, and for fraud, the malice or evil intent of its agent being imputed to it; and that it may also be held liable in a civil action for assault and battery; and that exemplary or punitive damages may be recovered in proper cases.³⁸ There is a strong tendency in some jurisdictions to

Cas. 70; *Com. v. Proprietors of New Bedford Bridge*, 2 Gray (Mass.) 339; *State v. Passaic Co. Agricultural Soc.*, 54 N. J. Law, 260, 23 Atl. 680; *Com. v. Pulaski Co. Agricultural & Mechanical Ass'n*, 92 Ky. 197, 17 S. W. 442.

³⁴ *Reg. v. Great North of England Ry. Co.*, supra; *Com. v. Proprietors of New Bedford Bridge*, supra; *Louisville & N. R. Co. v. State*, 3 Head (Tenn.) 523; *State v. Louisville & N. R. Co.*, 91 Tenn. 445, 19 S. W. 229; *St. Louis, A. & T. Ry. Co. v. State*, 52 Ark. 51, 11 S. W. 1035; *State v. Chicago, M. & St. P. Ry. Co.*, 77 Iowa, 442, 42 N. W. 365; *State v. Roanoke Railroad & Lumber Co.*, 109 N. C. 860, 13 S. E. 719; *State v. Monongahela R. R. Co.*, 37 W. Va. 108, 16 S. E. 519; *Chicago & E. I. R. Co. v. People*, 44 Ill. App. 632; *Delaware Division Canal Co. v. Com.*, 60 Pa. St. 367; *Northern Cent. R. Co. v. Com.*, 90 Pa. St. 305; *Pittsburgh & Allegheny Bridge Co. v. Com.* (Pa. Sup.) 8 Atl. 217; *Palatka & I. R. R. Co. v. State*, 23 Fla. 546, 3 South. 158; *Savannah, F. & W. Ry. Co. v. State*, 23 Fla. 579, 3 South. 204; *State v. Warren R. Co.*, 29 N. J. Law, 353; *State v. Central R. Co.*, 32 N. J. Law, 220.

³⁵ *State v. Passaic Co. Agricultural Soc.*, 54 N. J. Law, 260, 23 Atl. 680.

³⁶ *Com. v. Pulaski Co. Agricultural & Mechanical Ass'n*, 92 Ky. 197, 17 S. W. 442.

³⁷ *Com. v. Proprietors of New Bedford Bridge*, 2 Gray (Mass.) 339.

³⁸ Ante, p. 197.

extend this doctrine so as to include criminal prosecutions. Dr. Wharton says that there is no good reason why the same acts for which corporations are subject to civil suit may not equally be the basis of criminal proceedings, when they result in injury to the public at large.³⁹ And it has been said in a late New Jersey case, after adverting to the fact that a corporation is civilly liable for malicious wrongs: "It is difficult, therefore, to see how a corporation may be amenable to civil suit for libel and malicious prosecution and private nuisance, and be mulcted in exemplary damages, and at the same time not be indictable for like offenses where the injury falls upon the public. That malice and evil intent may be imputed to corporations has been repeatedly adjudged."⁴⁰

There are no cases thus far in which a corporation has been held liable criminally for malicious wrongs, or for wrongs involving a specific evil intent, or for wrongs involving the element of personal violence. On the contrary, actual authority, as far as it goes, is against any such doctrine.⁴¹

Contempt of Court.

A corporation may be guilty of a contempt of court by reason of acts or omissions of its officers, as where they violate an injunction. And in such a case it is well settled that the court has the same power to punish it by a fine, as it would have in the case of a natural person.⁴²

³⁹ 1 Whart. Cr. Law, § 87.

⁴⁰ State v. Passaic Co. Agricultural Soc., 54 N. J. Law, 260, 23 Atl. 680.

⁴¹ See Clark, Cr. Law, 79; Orr v. Bank, 1 Ohio, 38; Com. v. Proprietors of New Bedford Bridge, 2 Gray (Mass.) 339.

⁴² People v. Albany & V. R. Co., 12 Abb. Prac. (N. Y.) 171; Golden Gate Consolidated Hydraulic Min. Co. v. Superior Court, 65 Cal. 187, 3 Pac. 628; Mayor, etc., of New York v. New York & Staten Island Ferry Co., 64 N. Y. 624; U. S. v. Memphis & L. R. R. Co., 6 Fed. 237.

CHAPTER VIII.

THE CORPORATION AND THE STATE.

- 73-74. Power of the State over Corporations—Charter as a Contract.
- 75. Police Power of the State.
- 76. Power of Eminent Domain.
- 77. Reservation of Power to Repeal or Amend Charter.
- 78. Offer of Amendment—Power of Majority.
- 79-81. Taxation of Corporations.

POWER OF THE STATE OVER CORPORATIONS—CHARTER AS A CONTRACT.

73. The charter of a private corporation involves a contractual obligation within the meaning of the constitutional declaration that no state shall pass any law impairing the obligation of contracts, and it cannot be impaired by repeal or amendment contrary to its terms.
- (a) There is a contract between the corporation and the state which cannot be so impaired.
 - (b) There is also a contract between the corporators and the corporation, which cannot be impaired.
 - (c) But repeal or amendment of a charter is not unconstitutional as impairing the obligation of contracts between the corporation and third persons.
74. The constitutional provision referred to does not prevent legislation affecting the charter of a corporation under the following circumstances:
- (a) It does not prevent the state from passing laws in the valid exercise of its police power.
 - (b) It does not prevent the state from taking the property and franchises of a corporation for public use, under the power of eminent domain, if due compensation is made.

- (c) It does not prevent the repeal, alteration, or amendment of a charter, if the power to repeal, alter, or amend was reserved by the state in granting the charter.

Theoretically, the British parliament, with respect to its power to enact laws, is omnipotent. There is no written constitution imposing restraints upon it. And, among other unlimited powers, it has the power to repeal or alter charters of corporations, as it may see fit. The power is not often exercised, it is true, but it exists, and at certain periods of English history it has been arbitrarily exercised. Parliament, if it should choose, could grant a charter, and then, after the corporators have invested their money in the enterprise, repeal it, however great the loss might be. In this country the power of the legislature is not supreme, but is restricted in very many respects by constitutional provisions. In the constitution of the United States it is declared that "no state shall pass any law impairing the obligation of contracts."¹ And it is now settled beyond any controversy that the charter of a private corporation is a contract, within the meaning of the constitution.² In the Dartmouth College Case,³ a charter had been granted by the king of England to the trustees of Dartmouth College, a charity founded by private persons. Nearly forty years afterwards the legislature of New Hampshire undertook to alter this charter in material respects. The New Hampshire court sustained the act, but the decision was reversed by the supreme court of the United States, on the ground that the charter was a contract within the meaning of the constitution, and that the acts in question, in materially altering it,

¹ Const. U. S. art. 1, § 10.

² Trustees of Dartmouth College v. Woodward, 4 Wheat. 518, 1 Cumming, Cas. Priv. Corp. 490, W. D. Smith, Cas. Corp. 148, Shep. Cas. Corp. 248; Hazen v. Bank, 1 Sneed (Tenn.) 115; Zimmer v. State, 30 Ark. 677; Downing v. Board, 129 Ind. 443, 28 N. E. 123, 614; Ruggles v. People, 91 Ill. 256; Illinois Cent. R. Co. v. People, 95 Ill. 313; State v. Greer, 78 Mo. 188; Hamilton v. Keith, 5 Bush (Ky.) 458; Cary Library v. Bliss, 151 Mass. 364, 25 N. E. 92; and cases hereafter cited and referred to. Contra, Mechanics' & Traders' Branch of State Bank v. Debolt, 1 Ohio St. 591; Bank of Toledo v. City of Toledo, 1 Ohio St. 622; Skelly v. Bank, 9 Ohio St. 606.

³ Supra.

without the consent of the corporation, impaired its obligation, and were void.

The constitutional prohibition against acts impairing the obligation of contracts applies only in the case of private corporations. The charters of public corporations may be repealed or amended by the legislature at pleasure. As we have seen, however, colleges, hospitals, asylums, and other charitable institutions, founded by private means, are private corporations, and within the protection of the constitution, though they may have been founded for the benefit of the public.⁴

If the legislature, without having reserved the right to do so, repeals the charter of a corporation outright, there can be no question but that the repeal is unconstitutional and void. Difficult questions, however, arise where the charter is not repealed, but merely altered or amended. The rule in such cases is that, if the legislature alters the charter of a corporation in any material respect, it impairs the obligation thereof, unless the alteration or amendment is authorized under the rules hereafter shown. In the Dartmouth College Case,⁵ above referred to, the charter of the corporation vested the whole power of governing the college, of appointing and removing tutors, of fixing their salaries, of directing the course of study to be pursued by the students, and of filling up vacancies created in their own body, in the trustees appointed by the charter, and the charter expressly stipulated that the corporation, thus constituted, should continue forever, and that the number of trustees should forever consist of twelve, and no more. The acts of the legislature of New Hampshire increased the number of trustees to twenty-one, gave the appointment of the additional members to the executive of the state, and created a board of overseers, to consist of twenty-five persons, of whom twenty-one were to be appointed by the executive of the state, with the power to inspect and control the acts of the trustees. It was held that this was a material alteration of the charter, and that the acts therefore were void.⁶

⁴ Dartmouth College v. Woodward, *supra*; Downing v. Board, *supra*; Cary Library v. Bliss, *supra*; ante, p. 29.

⁵ *Supra*.

⁶ See, also, Downing v. Board, 129 Ind. 443, 28 N. E. 123, 614; Cary Library v. Bliss, 151 Mass. 364, 25 N. E. 92. In Zimmer v. State, 30 Ark. 677, by the terms

Alteration of a charter, where the power has not been reserved, is unconstitutional if it impairs the contracts between the corporation and the stockholders or members. Thus, where the charter of a corporation is not subject to alteration, amendment, or repeal, the legislature cannot change or interfere with the mode of voting at corporate meetings, as by allowing cumulative voting, etc.⁷ Nor can it authorize a majority of the stockholders or members to accept amendments of the charter, or to engage in enterprises not authorized by the charter, without the consent of the minority,⁸ or to consolidate with another corporation, and transfer the corporate property to it.⁹ Nor can a charter be altered by requiring a less amount of capital stock, so as to make previous subscribers liable as shareholders before the amount of stock required at the time of their subscription is subscribed.¹⁰ Such alterations and amendments as these are unconstitutional, not as impairing the implied contract between the corporation and the state, but as impairing the contract between the corporation and the dissenting members by compelling them to embark in an enterprise different from that agreed upon.

As we have seen in a former chapter, it is a settled rule for the construction of charters that in case of ambiguity and doubt they are to be construed most strictly in favor of the public and against the corporation. And this rule is important in connection with the subject now under discussion.¹¹

The state, in granting a charter to a private corporation, does not impliedly stipulate that it will not afterwards create a similar cor-

of an irrepensible charter, the corporation was authorized to form a union or consolidate with another corporation; and its officers, agents, and servants were exempted from military and road duty, and from jury service. It was held that it could not be deprived of any of these privileges and exemptions by subsequent legislation.

⁷ *State v. Greer*, 78 Mo. 188; *Hays v. Com.*, 82 Pa. St. 518. Compare *New Haven & D. R. Co. v. Chapman*, 38 Conn. 56.

⁸ *Zabriskie v. Railroad Co.*, 18 N. J. Eq. 178, 1 Cumming, Cas. Priv. Corp. 781; *New Orleans, J. & G. N. R. Co. v. Harris*, 27 Miss. 517; *Black v. Canal Co.*, 24 N. J. Eq. 455.

⁹ *Lauman v. Railroad Co.*, 30 Pa. St. 46.

¹⁰ *Oldtown & L. R. Co. v. Veazie*, 39 Me. 571.

¹¹ See *Proprietors of Charles River Bridge v. Proprietors of Warren Bridge*, 11 Pet. 420, 1 Cumming, Cas. Priv. Corp. 506; ante, p. 125.

poration to compete with the former, or pass any other valid law, which will have the effect of rendering the first charter valueless. So long as it does not impair the obligation of its contract with the first corporation, as embodied in the charter, it may pass any valid law it may see fit, though the effect of such law may be to render the charter practically worthless. In *Proprietors of the Charles River Bridge v. Proprietors of the Warren Bridge*,¹² the state of Massachusetts had chartered the plaintiff to build a bridge across the Charles river, and to take tolls for the use thereof. After the bridge had been built and maintained for a number of years, the state chartered the defendant corporation, and authorized it to build another bridge over the Charles river in close proximity to the plaintiff's bridge, and under the defendant's charter its bridge in the course of a few years became the property of the state, and a free bridge. It was held that the defendant's charter was valid, though its effect was to indirectly destroy the value of the plaintiff's charter, franchises, and property, since the state did not expressly bind itself not to authorize another bridge, and no such stipulation could be implied. And so the state may charter a railroad or turnpike company to run its road along the same route as a previously chartered railroad, turnpike, or canal company, provided no exclusive privileges have been in terms granted to the prior corporation.¹³

In the absence of constitutional limitations, however, the legislature may grant an exclusive privilege to a private corporation,¹⁴ and, if it does so in its charter, the grant constitutes a contract in the sense of the federal constitution, and cannot be impaired by subsequent legislation.¹⁵ Thus where a state created a corporation to construct a bridge, and the charter expressly stipulated that no other bridge should be built within a certain distance of it, a sub-

¹² 11 Pet. 420, 1 Cumming, Cas. Priv. Corp. 508. And see *In re Opening of Hamilton Avenue*, 14 Barb. (N. Y.) 405.

¹³ *White River Turnpike Co. v. Vermont Cent. R. Co.*, 21 Vt. 590; *Tuckahoe Canal Co. v. Tuckahoe & J. River R. Co.*, 11 Leigh (Va.) 42; *Washington & B. Turnpike Co. v. Baltimore & O. R. Co.*, 10 Gill & J. (Md.) 392.

¹⁴ Ante, p. 36.

¹⁵ *New Orleans Gaslight Co. v. Louisiana Light & Heat Producing & Manuf'g Co.*, 115 U. S. 650, 6 Sup. Ct. 252.

sequent charter authorizing another corporation to construct a bridge within the prohibited distance was held unconstitutional.¹⁶ The same rule applies where the legislature charters a gas, or water, or electric lighting company, and grants it an exclusive privilege of supplying a city and its inhabitants with light or water.¹⁷ In some states the constitution now restricts the power of the legislature to grant exclusive privileges.¹⁸

The repeal of a charter or dissolution of a corporation under statutory authority is not a violation of the federal constitution as impairing the obligation of contracts made by the company with third persons.¹⁹ Two reasons for so holding were given by the supreme court of the United States in *Mumma v. Potomac Co.*²⁰ In the first place, the obligation of the contracts of the company survives the dissolution, and the creditors may enforce their claims against any property belonging to the company which has not passed into the hands of bona fide purchasers, but is still held in trust for the company, or for the stockholders, at the time of its dissolution in any mode permitted by the local laws. In the second place, it was said, "independently of this view of the matter, it would be extremely difficult to maintain the doctrine contended for by the plaintiff in error upon general principles. A corporation, by the very terms and nature of its political existence, is subject to dissolution by a surrender of its corporate franchises, and by a forfeiture of them for willful misuser and nonuser. Every creditor must be presumed to understand the nature and incidents of such a body politic, and to contract with reference to them. And it would be a doctrine new in the law that the existence of a private contract of the corporation should force upon it perpetuity of existence contrary to public policy, and the nature and objects of its charter."

"There is a distinction between the obligation of a contract and

¹⁶ *The Binghamton Bridge*, 3 Wall. 51.

¹⁷ *New Orleans Gaslight Co. v. Louisiana Light & Heat Producing & Manuf'g Co.*, *supra*; *New Orleans Waterworks Co. v. Rivers*, 115 U. S. 674, 6 Sup. Ct. 273.

¹⁸ See *ante*, p. 36.

¹⁹ *Mumma v. Potomac Co.*, 8 Pet. 281, 1 Cumming, Cas. Priv. Corp. 459; *Thornton v. Railway Co.*, 123 Mass. 32, 1 Cumming, Cas. Priv. Corp. 462; *Read v. Frankfort Bank*, 23 Me. 318.

²⁰ 8 Pet. 281, 1 Cumming, Cas. Priv. Corp. 459.

the remedy for its enforcement. Whatever pertains merely to the remedy may be changed or modified, at the discretion of the legislature, without impairing the obligation of the contract, provided the remedy be not wholly taken away, nor so hampered or reduced in effectiveness as to render the contract practically incapable of enforcement."²¹ This principle applies to laws affecting existing corporations, the charters of which are not subject to alteration, amendment, or repeal by the legislature. Thus a statute which prescribes a mode of service of judicial process upon a corporation, different from that provided for in its charter, or which otherwise authorizes new remedies, is not void as impairing the obligation of a contract.²²

POLICE POWER OF THE STATE.

75. There is nothing in the federal or state constitutions depriving the legislatures of the power to pass any laws, in the exercise of the police power of the state, which may be necessary or proper for the protection of the public safety, health, comfort, morals, or the property of the citizens; and such laws are valid, though they may detract from the powers of existing corporations, or impose burdens upon them. The legislature cannot divest itself of this power.

In this country the legislatures of the different states have the same unlimited power in regard to legislation as the British parliament, except in so far as they may be restrained by the state or federal constitution. They can pass any law affecting existing corporations, however much it may increase their burdens or restrict their powers, provided no constitutional provision is violated.²³ The constitutional provision against laws impairing the obligation of contracts does not prevent the legislatures from regulating corporations,

²¹ Black, Const. Law, 538.

²² *Cairo & F. R. Co. v. Hecht*, 95 U. S. 168. See, also, *Carey v. Giles*, 9 Ga. 253; *Chicago Life Ins. Co. v. Auditor of Public Accounts*, 101 Ill. 82.

²³ *Thorpe v. Railroad Co.*, 27 Vt. 140, 1 Cumming, Cas. Priv. Corp. 521.

under the police power of the state, in the use of their franchises.²⁴ The constitution was not intended to deprive the legislatures of this power, and the legislatures could not divest themselves of it if they would. "Whatever differences of opinion," it has been said, "may exist as to the extent and boundaries of the police power, and however difficult it may be to render a satisfactory definition of it, there seems to be no doubt that it does extend to the protection of the lives, health, and property of the citizens, and to the preservation of good order and the public morals. The legislature cannot, by any contract, divest itself of the power to provide for these objects. They belong emphatically to that class of objects which demand the application of the maxim, 'Salus populi suprema lex;' and they are to be attained and provided for by such appropriate means as the legislative discretion may devise. That discretion can no more be bargained away than the power."²⁵

It may be laid down as a general rule that the legislature may control the action of corporations, prescribe their functions and duties, and impose restraints upon them, to the same extent as upon natural persons, in all matters coming within the general range of legislative authority; subject to the limitation of not impairing the obligation of contracts, provided the essential franchise is not taken away without compensation.²⁶ Nothing is better settled than that, under its police power, a state may subject persons to restraints and burdens in order to secure the general comfort, health, and prosperity of the people at large; and this power extends to corporations as well as to natural persons. Thus, if the state creates a corporation and authorizes it to erect a powder mill, or to maintain a burying ground, or a slaughterhouse, fertilizer manufactory, or tannery at a certain place, at a time when the place is remote from inhabitants, it may afterwards require the business to be suspended or removed,

²⁴ Thorpe v. Railroad Co., 27 Vt. 140, 1 Cumming, Cas. Priv. Corp. 521; Beer Co. v. Massachusetts, 97 U. S. 25, 1 Cumming, Cas. Priv. Corp. 533; Answer of the Justices, 9 Cush. (Mass.) 604; Galena & C. U. R. Co. v. Loomis, 13 Ill. 548, 56 Am. Dec. 471; Chicago Life Ins. Co. v. Needles, 113 U. S. 574, 5 Sup. Ct. 681; Eagle Ins. Co. of Cincinnati v. State of Ohio, 153 U. S. 446, 14 Sup. Ct. 868.

²⁵ Beer Co. v. Massachusetts, 97 U. S. 25, 1 Cumming, Cas. Priv. Corp. 533. And see Town of Lake View v. Rose Hill Cemetery Co., 70 Ill. 191.

²⁶ Thorpe v. Railroad Co., 27 Vt. 140, 1 Cumming, Cas. Priv. Corp. 521; Ward v. Farwell, 97 Ill. 593.

or secured from doing harm, at the sole expense of the corporation, if in process of time dwellings approach the locality, so as to render the further pursuit or maintenance of the business at that place destructive to the health or comfort of others.²⁷

In *Boston Beer Co. v. Massachusetts*²⁸ a corporation had been chartered to manufacture and sell malt liquors. Afterwards the legislature passed a prohibitory liquor law, and it was contended by the corporation that this law, if applicable to it, was void, as being an impairment of its contract with the state. The court held the law valid as to the corporation, on the ground that, though it was given by its charter the right to manufacture and sell malt liquors, the charter could not be construed as conferring any greater or more sacred right than any citizen had to manufacture malt liquor; nor as exempting the corporation from any control therein to which a citizen would be subject, if the interests of the community should require it. "If the public safety or the public morals," it was said, "require the discontinuance of any manufacture or traffic, the hand of the legislature cannot be stayed from providing for its discontinuance by any incidental inconvenience which individuals or corporations may suffer. All rights are held subject to the police power of the state." Other illustrations are given below.²⁹

²⁷ *Thorpe v. Railroad Co.*, *supra*; *Fertilizing Co. v. Hyde Park*, 97 U. S. 659; *Coates v. Mayor, etc., of New York*, 7 Cow. (N. Y.) 585; *Brick Presbyterian Church v. Mayor, etc., of New York*, 5 Cow. (N. Y.) 538; *Town of Lake View v. Rose Hill Cemetery Co.*, 70 Ill. 191.

²⁸ 97 U. S. 25, 1 Cumming, Cas. Priv. Corp. 533.

²⁹ The state cannot prohibit existing railroad companies from carrying unobjectionable freight and passengers; but it may regulate them in the conduct of their business, so as to secure the safety of persons and property. It is perfectly competent, therefore, for the legislature to prohibit them from carrying persons or live stock infected with contagious diseases, or to require them to stop at crossings, to maintain switchmen and watchmen, to provide a certain number of brakemen, to use proper rails and maintain a proper track, or to maintain fences and cattle guards along their road; and it may require them to bear the expense of such safeguards. *Thorpe v. Railroad Co.*, 27 Vt. 140, 1 Cumming, Cas. Priv. Corp. 521; *Com. v. Eastern R. Co.*, 103 Mass. 254, 1 Cumming, Cas. Priv. Corp. 546; *Nelson v. Railroad Co.*, 26 Vt. 717; *Galena & C. U. R. Co. v. Loomis*, 13 Ill. 548, 56 Am. Dec. 471; *Horn v. Railway Co.*, 38 Wis. 463; *Ohio & M. R. Co. v. McClelland*, 25 Ill. 140; *Hegeman v. Railroad Corp.*, 16 Barb. (N. Y.) 353. And it may require a railroad company to stop at county seats to take on and let off passengers. Chi-

In the exercise of the police power the state cannot, in the case of a corporation, any more than in the case of a natural person, pass any law taking or destroying property which is actually in existence, and in which the right of the owner has become vested,

Chicago & A. R. Co. v. People, 105 Ill. 657. And it may require a railroad company, at its own expense, to construct a bridge over a highway, even though it may not have reserved the power to amend or repeal its charter. *People v. Boston & A. R. Co.*, 70 N. Y. 569. And it may prohibit railroad companies from crossing each others' tracks at grade. *Pittsburg & C. R. Co. v. Southwest P. Ry. Co.*, 77 Pa. St. 173. So a city ordinance may prohibit existing railroad companies from running steam engines on a certain street. *Railroad Co. v. Richmond*, 96 U. S. 521. The state, having chartered a bank with power to receive money on deposit, and pay away the same, and to discount bills of exchange, and make loans, could not afterwards make it unlawful for the bank to transfer by indorsement or otherwise any bill or note, etc., for this would be a violation of the charter, and not at all necessary as a police measure. *Jemison v. Bank*, 23 Ala. 168. But the state may bind existing savings banks, or other banks, by general laws relating to investments of deposits. *Answer of the Justices to Inquiry of the Senate*, 9 Cush. (Mass.) 604. And it has been held that it may pass a law making stockholders of existing corporations liable for the future debts of the corporation. *Child v. Coffin*, 17 Mass. 64; *Gray v. Coffin*, 9 Cush. (Mass.) 192; *Stanley v. Stanley*, 28 Me. 191. And it may reduce the rate of interest, or prohibit speculations in exchange, or depreciated paper, or the issuing of bills of a given denomination, etc. See *Thorpe v. Railroad Co.*, 27 Vt. 140, 1 Cumming, Cas. Priv. Corp. 521. The state has the same power to tax corporations as it has to tax individuals, provided it has not expressly surrendered the right in granting the charter, though the power clearly abridges the beneficial use of the franchise, and is capable of being so exercised as virtually to destroy it. *Providence Bank v. Billings*, 4 Pet. 514; *post*, p. 219. The right to have migratory fish pass in their accustomed course up and down rivers and streams is a public right, and may be regulated and protected by the legislature in such a manner as it may deem appropriate; and every grant of a right to maintain a mill dam across a stream where such fish are accustomed to pass is subject to the implied condition or limitation that a sufficient and reasonable way shall be allowed for the fish, unless cut off by express provision or obvious implication in the grant. *Commissioners on Inland Fisheries v. Holyoke, Water-Power Co.*, 104 Mass. 446; *Com. v. Essex Co.*, 13 Gray (Mass.) 239, 1 Cumming, Cas. Priv. Corp. 550. The state may pass a law requiring existing corporations, like insurance companies, banks, etc., having extensive dealings with the public, to make periodical statements of their condition, and providing for compulsory liquidation of their business in case of insolvency; or make other provisions of this nature for the protection of the public. Such laws are valid police regulations. *Attorney General v. North America Life Ins. Co.*, 82 N. Y. 172; *Chicago Life Ins. Co. v. Needles*, 113 U. S. 574, 5 Sup. Ct. 681; *Eagle Ins. Co. v.*

even though the law may be for the public good, unless it makes due compensation therefor. Thus, if the state were to charter a corporation unqualifiedly for the purpose of manufacturing and selling malt liquors, it could not afterwards pass a liquor law prohibiting the sale of liquors already manufactured by the corporation without making due compensation therefor, though it could prohibit further manufacture.⁸⁰

So, the right of members to vote at corporate meetings for directors, and on other corporate matters, is a property right, and, if the mode of voting is prescribed by an irrepealable charter, it is protected by the constitutional prohibition against laws impairing the obligation of contracts, so that the state cannot interfere with it either by constitutional or legislative enactment. A law regulating the mode of voting at corporate elections cannot be called a police regulation.⁸¹

POWER OF EMINENT DOMAIN.

76. The property of a corporation, including its franchises, may, like the property of an individual, be taken for public use under the power of eminent domain, on making due compensation therefor.

The power of the state to take private property for public use under the power of eminent domain, on making compensation to the owner, extends to the property and franchises of a corporation, as well as the property of individuals. "The property of corporations, including their franchises, may be taken for public use under the

Ohio, 153 U. S. 446, 14 Sup. Ct. 868; Ward v. Farwell, 97 Ill. 593; Chicago Life Ins. Co. v. Auditor of Public Accounts, 101 Ill. 82. Railroad companies may be made liable to laborers employed by contractors in constructing their roads. Branin v. Railroad Co., 31 Vt. 214. And a state may regulate the charges of railroad and warehouse companies, and other corporations engaged in a public employment affecting the public interest. Munn v. Illinois, 94 U. S. 113; Chicago, B. & Q. R. Co. v. Iowa, Id. 155; Stone v. Trust Co., 116 U. S. 307, 6 Sup. Ct. 334, 388, 1191; Ruggles v. People, 91 Ill. 256; Illinois Cent. R. Co. v. People, 95 Ill. 313. But the regulation must be reasonable. Stone v. Trust Co., supra.

⁸⁰ Beer Co. v. Massachusetts, 97 U. S. 25, 1 Cumming, Cas. Priv. Corp. 533. And see Planters' Bank v. Sharp, 6 How. 301.

⁸¹ State v. Greer, 78 Mo. 188.

power of eminent domain, on making due compensation.”³² Thus, where the legislature, under a reserved power, repealed the charter of a railroad company operating a railroad through the streets of a city, it was held that in chartering another corporation it had the power to authorize it to take the property of the old corporation, on making due compensation therefor.³³

Laws which take or authorize the taking of corporate property and franchises for public use under the power of eminent domain, which cannot legally be done without making compensation, must be distinguished from laws regulating corporations in the use of their franchises and property, enacted either under the police power of the state, or under a power to alter or amend the charter reserved by the state in granting it. Police regulations, as we have seen, may impose burdens and expenses upon corporations for the public good, but this does not form ground for objection by the corporation.³⁴

RESERVATION OF POWER TO REPEAL OR AMEND CHARTER.

77. The state may, and generally does, reserve the power to repeal, alter, or amend charters by a provision to that effect either in the charter itself, or act of incorporation, or in some general law, or in the constitution. This reservation, however, gives no right to impair or take away vested rights.

The state may always, in granting a charter, incorporate such terms and conditions as it may see fit. Therefore it may reserve the power to alter, amend, or repeal the charter. And it may do so

³² *Greenwood v. Freight Co.*, 105 U. S. 13, 1 Cumming, Cas. Priv. Corp. 538, W. D. Smith, Cas. Corp. 160, Shep. Cas. Corp. 260. And see *West River Bridge Co. v. Dix*, 6 How. 507; *Eastern R. Co. v. Boston & M. R. R.*, 111 Mass. 125; *White River Turnpike Co. v. Vermont Cent. R. Co.*, 21 Vt. 590; *Boston Water-Power Co. v. Boston & W. R. Corp.*, 23 Pick. (Mass.) 360; *Central Bridge Corp. v. City of Lowell*, 4 Gray (Mass.) 474; *Tuckahoe Canal Co. v. Tuckahoe & J. R. R. Co.*, 11 Leigh (Va.) 42; *Black v. Canal Co.*, 24 N. J. Eq. 455; *Board of Trustees of Illinois & M. Canal v. Chicago & R. I. R. Co.*, 14 Ill. 314.

³³ *Greenwood v. Freight Co.*, supra.

³⁴ Ante, p. 207. See *Com. v. Eastern R. Co.*, 103 Mass. 254, 1 Cumming, Cas. Priv. Corp. 546.

either by incorporating such a condition in the charter itself, or by a general law in force at the time the charter is granted, or by a provision contained in the state constitution. In the two latter cases no reference need necessarily be made in the charter to the general law or constitutional provision. If it is applicable, it becomes a part of the charter, and a term of the contract between the state and the corporators.³⁵

Where a general law provides, as in many states, that charters shall be subject to amendment, alteration, or repeal, "at the pleasure of the legislature," the reason of a repeal or amendment and the motive of the legislature are immaterial. "The validity of such action does not depend on the necessity for it, or on the soundness of the reasons which prompted it."³⁶

As shown in a previous chapter, an amendment, like the original charter, must be accepted, to have any effect. Though the legislature may have reserved the power to alter, amend, or repeal a charter of a private corporation, and though, under this reservation of power, it can repeal the charter without regard to the consent or nonconsent of the corporation, and may impose an amendment as a condition of the corporation's continuing to exercise its franchises, it cannot, without its consent, compel it to continue under the charter as amended. The amendment must be accepted, or it has no binding force. As was said by the Massachusetts court, "that a man may refuse a grant, whether from the government or an individual, seems to be a principle too clear to require the support of authorities."³⁷ Of course, a corporation cannot conduct its opera-

³⁵ *Greenwood v. Freight Co.*, 105 U. S. 13, 1 Cumming, Cas. Priv. Corp. 538, W. D. Smith, Cas. Corp. 160, Shep. Cas. Corp. 260; *Beer Co. v. Massachusetts*, 97 U. S. 25, 1 Cumming, Cas. Corp. 533; *Com. v. Eastern R. Co.*, 103 Mass. 254, 1 Cumming, Cas. Priv. Corp. 546; *Parker v. Railroad Co.*, 109 Mass. 506; *Miller v. State*, 15 Wall. 478; *Jackson v. Walsh*, 75 Md. 304, 23 Atl. 778; *Story v. Plank-Road Co.*, 16 N. J. Eq. 13; *State v. Commissioner of Railroad Taxation*, 37 N. J. Law, 228.

³⁶ *Greenwood v. Freight Co.*, supra; *Com. v. Eastern R. Co.*, supra. And see *Lothrop v. Stedman*, 42 Conn. 584.

³⁷ *Ellis v. Marshall*, 2 Mass. 279. See *Yeaton v. Bank*, 21 Grat. (Va.) 593. In this case it is said: "Every amendment or modification of a charter of incorporation is nothing more than a new contract, which is not binding upon the corporate body until accepted by them." See ante, p. 53, and cases there cited.

tions in defiance of the state; and, if it does not accept an authorized amendment of its charter, it must discontinue its operations as a corporate body.³⁸ And, as we have seen, if a corporation continues to act as such after an authorized amendment, it may be regarded as having accepted the amendment.³⁹

The state, under a reservation of power to repeal, alter, or amend a charter, may exercise such power, and to almost any extent, to carry into effect the original purposes of the grant, and to protect the rights of the public and the corporators, or to promote the due administration of the affairs of the corporation; but it cannot impair or destroy vested rights under such a reservation of power.⁴⁰ In a case in which the legislature prescribed the rate of fare to be charged by an existing railroad company, whose charter was subject to alteration, amendment, or repeal, Mr. Justice Swayne said: "It is urged that the franchise here in question was properly held by a vested right, and that its sanctity as such could not be thus invaded. The answer is, 'Consensus facit jus.' It was according to the agreement of the parties. The company took the franchise subject expressly to the power of alteration or repeal by the general assembly. There is, therefore, no ground for just complaint against the state. Where an act of incorporation is repealed, few questions of difficulty can arise. Equity takes charge of all the property and effects which survive the dissolution, and administers them as a trust fund, primarily for the benefit of creditors. If anything is left, it goes to the stockholders. Even the executory contracts of the defunct corporation are not extinguished. The power of alteration and amendment is not without limit. The alterations must be reasonable. They must be made in good faith, and be consistent with the scope and object of the act of incorporation. Sheer oppression and wrong cannot be inflicted under the guise of amend-

³⁸ Yeaton v. Bank, *supra*.

³⁹ Ante, p. 54, and cases there cited.

⁴⁰ See dissenting opinions of Strong, Bradley, and Field, JJ., in the Sinking-Fund Cases, 99 U. S. 700, 727. And see Sage v. Dillard, 15 B. Mon. (Ky.) 340. The legislature cannot impair the right to redeem from a mortgage. Ashuelot R. Co. v. Elliot, 58 N. H. 451. Nor can it prevent distribution of the assets of a corporation, whose charter it has repealed, among those who are entitled to them. Lothrop v. Stedman, 42 Conn. 584.

ment or alteration. Beyond the sphere of the reserved powers, the vested rights of property of corporations, in such cases, are surrounded by the same sanctions and are as inviolable as in other cases.”⁴¹ The court then held that the regulation in question did not take away a vested right, but was a legitimate exercise of the reserved power of alteration.

A corporation authorized to construct a dam across a river or stream may be afterwards required to construct and maintain fishways to permit the passage of migratory fish.⁴² But where such a corporation had built a fishway in its dam, as required by statute, and had afterwards been granted an enlargement of its charter, upon the consideration that it should pay the damage caused to the owners of fishing rights by the dam as already built, with a fishway known to the legislature to be insufficient, and the corporation paid such damages, it was held that the right to maintain the dam as it was, with the insufficient fishway, had been paid for, and was vested in the corporation, and that this vested right could not be taken from it by a subsequent act requiring it to construct sufficient fishways at great cost, though the legislature had reserved the right to alter, amend, or repeal the charter.⁴³

⁴¹ *Shields v. Ohio*, 95 U. S. 319. In another case it was said: “A power reserved to the legislature to alter, amend, or repeal a charter, authorizes it to make any alteration or amendment of a charter granted subject to it, which will not defeat or substantially impair the object of the grant, or any rights vested under it, and which the legislature may deem necessary to secure either that object or any public right.” *Close v. Glenwood Cemetery*, 107 U. S. 466, 2 Sup. Ct. 267. And see *State v. Neff*, 52 Ohio St. 375, 40 N. E. 720; *People v. O’Brien*, 111 N. Y. 1, 18 N. E. 692.

⁴² *Com. v. Essex Co.*, 13 Gray (Mass.) 239, 1 Cumming, Cas. Priv. Corp. 550; *Commissioners on Inland Fisheries v. Holyoke Water-Power Co.*, 104 Mass. 446.

⁴³ *Com. v. Essex Co.*, *supra*. The court said in this case: “No amendment or alteration of the charter can take away the property or rights which have become vested under a legitimate exercise of the powers granted. It appears to us, in the present case, that after the government, acting in behalf of the public, and also of all those riparian owners whose fish rights would be damaged by the defendant’s dam, with the fishway as it was, entered into a solemn and formal contract with the defendant company to exempt them from the obligation of making and maintaining a suitable and sufficient fishway, if such were practicable, by indemnifying all persons damaged in their several fisheries, and the defendant company had executed their part of the contract by the payment

So, where a corporation had built a plank road, and established a toll gate, as authorized by its charter, it was held that the reserved power to amend, alter, or repeal its charter did not give the legislature the right to require it to move the toll gate beyond the limits of a city which had grown up around it, and so to take from the company the right to collect tolls upon more than two miles of its road. "A statute which could have this effect," said Judge Cooley, "would not be a statute to amend franchises, but a statute to confiscate property; it would not be a statute of regulation, but of spoliation."⁴⁴

The power to alter, amend, or repeal a charter does not give the legislature the power to change the charter, and force a new and different charter upon the corporators. As was said in a New Jersey case: "It can repeal or suspend the charter; it can alter or modify it; it can take away the charter; but it cannot impose a new one, and oblige the stockholders to accept it. It can alter or modify the old one; but power to alter or modify anything can never be held to imply a power to substitute a thing entirely different. It is not the meaning of the words in their usually received sense. Power to alter a mansion house would never be construed to mean a power to tear down all but the back kitchen and front piazza, and build one three times as large in its place. In anything altered, something must be preserved to keep up its identity; and a matter of the same kind wholly or chiefly new, substituted for another, is not an alteration; it is a change."⁴⁵

Under the reservation of power to amend, alter, or repeal charters, it has been held that the legislature may make the stockholders of a corporation individually liable for its future debts;⁴⁶ that it may vary the measure, and thus enlarge the proportion, of the prof-

of a large sum of money, it was not competent for the legislature, without any change of circumstances, under their authority to amend and alter the charter of the company, to pass a law requiring them to do the acts from which, by the terms of such contract, they had been exempted, and therefore that the said act was null and void."

⁴⁴ *City of Detroit v. Detroit & H. P. R. Co.*, 43 Mich. 140, 5 N. W. 275, 1 Cumming, Cas. Priv. Corp. 560.

⁴⁵ *Zabriskie v. Railroad Co.*, 18 N. J. Eq. 178, 1 Cumming, Cas. Priv. Corp. 781, 790.

⁴⁶ *Sherman v. Smith*, 1 Black, 587; *In re Lee & Co.'s Bank*, 21 N. Y. 9; *Bailey*

its which a mutual life insurance company is required by the terms of its charter to pay a charitable institution;⁴⁷ that railroad companies may be compelled to make changes in the level, grade, and surface of the roadbed, new structures at crossings of other railroads or of highways, or station houses at particular places, in a manner and to be enforced by forms of process different from those provided for or contemplated by the original charter, or the general laws in force when the original charter was granted;⁴⁸ or to require a corporation authorized to build and maintain a dam across a navigable river to construct a lock for purposes of navigation;⁴⁹ or to require a corporation authorized to maintain a dam to maintain suitable fishways;⁵⁰ or to revoke an exemption from taxation, or increase a tax or license fee;⁵¹ or to require a corporation to establish a sinking fund to meet its obligations;⁵² or to authorize a city to subscribe for stock, and to appoint two directors;⁵³ or, according to some of the decisions, but not all, to authorize cumulative voting at stockholders' meetings at an election of directors;⁵⁴ or to increase the number of trustees of an incorporated college, in

v. Hollister, 26 N. Y. 112; *Gardner v. Insurance Co.*, 9 R. I. 194. In some states this is a legitimate exercise of the police power of the state. *Ante*, p. 210, note 29.

⁴⁷ *Massachusetts General Hospital v. State Mut. Life Assur. Co.*, 4 Gray (Mass.) 227.

⁴⁸ *City of Roxbury v. Boston & P. R. Co.*, 6 Cush. (Mass.) 424; *Fitchburg R. Co. v. Grand Junction R. & D. Co.*, 4 Allen (Mass.) 198; *Com. v. Eastern R. Co.*, 103 Mass. 254, 1 Cumming, Cas. Priv. Corp. 546; *Albany N. R. Co. v. Brownell*, 24 N. Y. 345 (overruling *Miller v. Railroad Co.*, 21 Barb. [N. Y.] 513). In *Mayor, etc., of Worcester v. Norwich & W. R. Co.*, 109 Mass. 103, the legislature had passed an act requiring certain railroad companies to unite in a passenger station in the city of Worcester, to extend their tracks in the city to the union station, and after the extension to discontinue parts of their existing locations. The act was held to be constitutional and valid, as it was a reasonable exercise of the reserved right to amend, alter, or repeal the charters of the corporations.

⁴⁹ *South Bay Meadow Dam Co. v. Gray*, 30 Me. 547.

⁵⁰ *Commissioners on Inland Fisheries v. Holyoke Water-Power Co.*, 104 Mass. 446.

⁵¹ *Post*, p. 228.

⁵² *Union Pac. R. Co. v. U. S.*, 99 U. S. 700.

⁵³ *New Haven & D. R. Co. v. Chapman*, 38 Conn. 56.

⁵⁴ *Cross v. Railway Co.*, 35 W. Va. 174, 12 S. E. 1071. But see *Orr v. Bracken Co.*, 81 Ky. 593; *Hays v. Com.*, 82 Pa. St. 518.

which the state is part owner, and to require a majority of them to consist of certain state officers, instead of being elected, as formerly, by the private stockholders;⁵⁵ or to regulate the charges of railroad companies, water companies, and other quasi public corporations.⁵⁶

A reserved power of amending or repealing the charter of a corporation is a legislative power, and cannot authorize the legislature to exercise judicial powers. This would be unconstitutional. For instance, it cannot authorize the legislature to foreclose a mortgage on the corporate property.⁵⁷ It may, however, appoint a receiver or trustee to settle the affairs of an insolvent corporation. This is a legislative act.⁵⁸ It is also perfectly competent for the legislature to reserve to itself the right to repeal a charter for a violation thereof or other default. Such a reservation is not a reservation of judicial power, and for that reason unconstitutional, for an inquiry by the legislature into the affairs or defaults of a corporation, with a view to discontinue it, is not a judicial act.⁵⁹

It has been held by some of the courts that, where the legislature reserves the power at any time to annul and vacate the charter of a corporation, if it shall fail to go into operation, or shall abuse or misuse its privileges, the legislature reserves the power of determining whether these contingencies have happened and a future legislature may repeal the charter without any judicial proceeding or prior notice.⁶⁰ But the weight of authority is against this view. Most of the courts have held that under such a reservation the investigation and determination of the question whether the occasion has arisen upon which the reserved power of the legislature may be exercised, is one of judicial, and not of legislative, cognizance, and that the power can be exercised only after a judicial investigation and determination, after notice to the corporation, and an opportunity to be heard.⁶¹ In some jurisdictions it is held that the

⁵⁵ *Jackson v. Walsh*, 75 Md. 304, 23 Atl. 778.

⁵⁶ *Shields v. Ohio*, 95 U. S. 319; *Spring Valley Waterworks v. Schottler*, 110 U. S. 347, 4 Sup. Ct. 48; *Parker v. Railroad Co.*, 109 Mass. 506.

⁵⁷ *Ashuelot R. Co. v. Elliot*, 58 N. H. 451.

⁵⁸ *Lothrop v. Stedman*, 42 Conn. 584; *Oarey v. Giles*, 9 Ga. 253.

⁵⁹ *Crease v. Babcock*, 23 Pick. (Mass.) 334; *Lothrop v. Stedman*, 42 Conn. 584.

⁶⁰ *Miners' Bank of Dubuque v. U. S.*, *Morris* (Iowa) 482.

⁶¹ *Flint & Fentonville Plank-Road Co. v. Woodbull*, 25 Mich. 99; *State v.*

legislature may exercise the power of repeal before a judicial investigation, and without notice, but that its action is subject to review by the courts.⁶²

Where a charter is offered before, but is not accepted until after, the adoption of a constitutional provision, or enactment of a statute, making all charters subject to amendment, alteration, or repeal, the provision enters into and forms a part of the contract between the corporation and the state, as the contract is not made until the charter is accepted.⁶³

78. OFFER OF AMENDMENT—POWER OF MAJORITY.

We are dealing here only with the power of the state to alter or amend a charter without the consent of the members of the corporation. Of course, there is nothing to prevent the legislature from authorizing a corporation to engage in new enterprises, if all the members see fit to accept the amendment. It is like the case where both parties to a contract rescind it by mutual agreement, and substitute a new contract. The power of the majority of the members to bind a dissenting minority by accepting an amendment of the charter thus offered will be discussed in a subsequent chapter.⁶⁴

TAXATION OF CORPORATIONS.

79. Unless a corporation is expressly exempted from taxation by its charter, the state may tax it to the same extent as it may tax individuals, without impairing the contract implied between the state and the corporation. But the power to tax is not unlimited. Thus:

(a) Taxes can be imposed only for a public purpose.

Noyes, 47 Me. 189; *Chesapeake & Ohio Canal Co. v. Baltimore & O. R. Co.*, 4 Gill. & J. (Md.) 122; *Regents of University of Maryland v. Williams*, 9 Gill & J. (Md.) 365.

⁶² *Erie & N. E. Railroad v. Casey*, 26 Pa. St. 287.

⁶³ *Attorney General v. Chicago & N. W. R. Co.*, 35 Wis. 599; *Stone v. Wisconsin*, 94 U. S. 181.

⁶⁴ *Post*, p. 447.

- (b) The taxing power is limited to persons, property, and business within the jurisdiction of the state.
 - (c) Provisions of the state constitution must not be violated, as provisions requiring uniformity and equality of taxation.
 - (d) In the absence of constitutional limitations, double taxation is not prohibited, but in a number of states it is prohibited by the constitution. Even when not prohibited, it is unjust, and in construing statutes all presumptions are against it.
 - (e) Provisions of the federal constitution must not be violated, such as
 - (1) The provision that no state shall deny to any person within its jurisdiction the equal protection of the laws. This prohibits unequal taxation.
 - (2) The provision that no state shall pass any law impairing the obligation of contracts. This prevents taxation of a corporation in violation of the express terms of its charter.
 - (3) As government bonds cannot be taxed, capital invested in them is exempt.
 - (4) No tax can be imposed which will amount to a regulation of or interference with interstate commerce.
 - (5) The states cannot interfere by taxation with the operation of corporations created by congress for the purpose of carrying into effect the constitutional powers of the federal government, except in so far as it may be permitted by congress.
80. By the weight of authority, a state, in creating a corporation, or afterwards for a consideration, but not otherwise, may agree that it shall be exempt from taxation, in whole or in part; and it cannot, in

such a case, impose a tax in violation of the charter without impairing the obligation of its contract. But

- (a) Exemption from taxation must be clearly shown. All presumptions are against it.
- (b) An exemption from taxation may be revoked if the state has reserved the power to repeal, alter, or amend the charter.

81. A corporation cannot escape liability for taxes on the plea of ultra vires.

Unless the case comes within one of the exceptions hereafter explained, a state has the same power to tax corporations as it has to tax natural persons, and no greater power than this. In the absence of express exemption from taxation, the imposition of a tax upon the property of a corporation is not a violation of its charter, and so within the constitutional prohibition against laws impairing the obligation of contracts, for exemption from taxation is not an implied term of the contract between the corporation and the state.⁶⁵

Object of Taxation.

The legislature can only use the power of taxation in aid of a public object, an object which is within the purpose for which governments are established. It cannot, therefore, be exercised in aid of private enterprises, even though the local public may be benefited in a remote or collateral way. Thus a tax cannot be imposed to aid a manufacturing enterprise of individuals.⁶⁶ This principle is not peculiar to the taxation of corporations. In *Lowell v. City of Boston* ⁶⁷ it was held that a statute authorizing the city of Boston to issue bonds, which, of course, might require taxation to pay them, and to lend the proceeds on mortgage to the owners of land, the buildings upon which were burned by the great fire of 1872, was unconstitutional.

⁶⁵ *Providence Bank v. Billings*, 4 Pet. 514. As to the taxation of railroad companies, see *State Railroad Tax Cases*, 92 U. S. 575-618; *Indianapolis & St. L. R. Co. v. Vance*, 96 U. S. 450; *Delaware Railroad Tax*, 18 Wall. 206.

⁶⁶ *Loan Association v. Topeka*, 20 Wall. 655; *City of Parkersburg v. Brown*, 106 U. S. 487, 1 Sup. Ct. 442.

⁶⁷ 111 Mass. 454.

Jurisdiction.

The power of taxation of a state is limited to persons, property, and business within her jurisdiction. All taxation must relate to one of these objects.⁶⁸ Bonds issued by a railroad company, for instance, are property in the hands of the holders, and, when held by non-residents of the state in which the company was incorporated, they cannot be taxed by the state, and it can make no difference that they are secured by a mortgage on land in the state.⁶⁹ A law, therefore, which requires a corporation to retain a certain percentage of the interest due on bonds made payable out of the state to citizens of another state, and held by them, is not a legitimate exercise of the taxing power.⁷⁰

Property Taxable.

The statutes generally provide very specifically what property of corporations shall be taxed, and how the taxes shall be assessed. But the construction of the statutes is not always clear. In corporations there are sometimes four elements of taxable value, namely: (1) The franchises of the corporation; (2) capital stock in the hands of the corporation; (3) corporate property, such as real estate, moneys, credits, and other personal property, other than such stock; and (4) shares of stock in the hands of the individual stockholders. Any one of these may be taxed, provided no constitutional limitations, federal or state, are violated. And where the shares of stock in a corporation are taxed, the legislature may require that the tax shall be paid by the corporation, and allow it to collect the same from the stockholders, or deduct it from dividends,⁷¹ unless the corporation, by its charter, is exempt from taxation, so that this might be a tax upon it.⁷²

⁶⁸ Case of State Tax on Foreign-Held Bonds, 15 Wall. 300; South Nashville St. R. Co. v. Morrow, 87 Tenn. 406, 11 S. W. 348; Com. v. Standard Oil Co., 101 Pa. St. 119; Com. v. Chesapeake & O. R. Co., 27 Grat. (Va.) 344.

⁶⁹ Case of State Tax on Foreign-Held Bonds, *supra*; South Nashville St. R. Co. v. Morrow, *supra*; Com. v. Chesapeake & O. R. Co., *supra*.

⁷⁰ Case of State Tax on Foreign-Held Bonds, *supra*.

⁷¹ Town of St. Albans v. National Car Co., 57 Vt. 68.

⁷² Post, p. 230, and note 111.

Double Taxation.

In many jurisdictions double taxation is prohibited by the constitution. In the absence of such prohibition, it is no doubt within the power of the legislature to assess taxes in such a way as to subject the corporation or the stockholders to double taxation.⁷³ But an intention to impose double taxes is never to be presumed. It is unjust, and therefore "all presumptions are against such an imposition."⁷⁴ Thus, where a charter exempted the stock of a corporation from taxation, but taxed its property, it was held that the exemption extended to shares of stock in the hands of the individual shareholders, the capital represented by which had been converted by the corporation into property which was liable to taxation.⁷⁵

A tax on the franchises of a corporation is not a tax on its property. Both may be taxed, and it will not be double taxation.⁷⁶ Some of the courts have held that the capital stock and the property of a corporation and the property of the individual shareholders in their shares are distinct property interests, and that the taxation of both does not amount to double taxation, and is authorized.⁷⁷ Other courts hold that this is double taxation, and in a number of states it is expressly provided that, where a corporation is taxed on its capital stock or property, the stockholders shall not be taxed on their shares.⁷⁸ In Maryland, by the declaration of rights, every owner of property is required to pay taxes in proportion to its actual

⁷³ See *Board of Revenue of Montgomery Co. v. Montgomery Gaslight Co.*, 64 Ala. 269; *Pittsburg, F. W. & O. R. Co. v. Com.*, 66 Pa. St. 77.

⁷⁴ *State of Tennessee v. Whitworth*, 117 U. S. 129, 6 Sup. Ct. 645, 647; *Wright v. Railroad Co.*, 64 Ga. 783; *Boston & Sandwich Glass Co. v. City of Boston*, 4 Metc. (Mass.) 181; *City of Fall River v. County Com'rs of Bristol*, 125 Mass. 567; *State v. Hannibal & St. J. R. Co.*, 37 Mo. 265.

⁷⁵ *State of Tennessee v. Whitworth*, *supra*.

⁷⁶ See *Manufacturers' Ins. Co. v. Loud*, 99 Mass. 146.

⁷⁷ *Ogden v. City of St. Joseph*, 90 Mo. 522, 3 S. W. 25; *Farrington v. Tennessee*, 95 U. S. 686; *Sturges v. Carter*, 114 U. S. 521, 5 Sup. Ct. 1014; *Bradley v. Bauder*, 36 Ohio St. 28; *South Nashville St. R. Co. v. Morrow*, 87 Tenn. 406, 11 S. W. 348; *State Bank of Virginia v. City of Richmond*, 79 Va. 113; *Danville Banking & Trust Co. v. Parks*, 88 Ill. 170; *Belo v. Commissioners*, 82 N. C. 415; *City of Memphis v. Ensley*, 6 Baxt. (Tenn.) 553.

⁷⁸ See article by Edward C. Moore, Jr., Esq., 10 Am. Law Rev. 755. See *Griffith v. Watson*, 19 Kan. 23; *Burke v. Badlam*, 57 Cal. 594; *Osborn v. Railroad Co.*, 40 Conn. 494; *Salem Iron Factory Co. v. Inhabitants of Danvers*, 10 Mass. 514.

worth. This has been held to prohibit double taxation, and it is held that the payment of a tax on the capital stock of a corporation is a bar to taxation on the corporate property, as the capital stock represents the whole property of the corporation; and this principle has been recognized in other states, though not in all.⁷⁹

Place of Taxation.

Personal property, including shares of stock, in the absence of any law to the contrary, follows the person of the owner, and has its situs at his domicile; but for the purposes of taxation it may be separated from him, and he may be taxed on its account at the place where it is actually located.⁸⁰ Shares of stock in a domestic corporation may therefore be taxed at the place within the state where the corporation is located, without regard to the place of residence of the holders; and the state may tax the shares of nonresidents as well as of residents.⁸¹ When a contrary rule is not declared by statute, the situs of shares of stock, for the purpose of taxation, is the residence of the owner.⁸² Shares in a foreign corporation may be taxed to a resident owner.⁸³

Restrictions in the Federal Constitution—Federal Corporations.

The constitution of the United States imposes some limitations upon the taxing power of the states. We can only mention these shortly, leaving the reader to follow up the subject by referring to works on taxation and constitutional law.

Under the constitutional provision that no state shall deny to any person within its jurisdiction the equal protection of the laws, a state cannot impose unequal taxation; but all taxes must be uniform,

⁷⁹ See 19 Am. Law Rev. 757; *State v. Sterling*, 20 Md. 520; *State v. Cumberland & P. R. Co.*, 40 Md. 22; *County Com'rs of Frederick Co. v. Farmers' & Mechanics' Nat. Bank*, 48 Md. 117; *Jones v. Davis*, 35 Ohio St. 474; *Whitney v. City of Madison*, 23 Ind. 331. Contra, *Lackawanna Iron & Coal Co. v. Luzerne Co.*, 42 Pa. St. 424.

⁸⁰ *Tappan v. Bank*, 19 Wall. 490.

⁸¹ So as to shares in national banks. 13 Stat. 112; *Tappan v. Bank*, 19 Wall. 490; *South Nashville St. R. Co. v. Morrow*, 87 Tenn. 406, 11 S. W. 348; *Town of St. Albans v. National Car Co.*, 57 Vt. 68.

⁸² *Ogden v. City of St. Joseph*, 90 Mo. 522, 3 S. W. 25.

⁸³ *Cooley, Tax'n*, 22; *Sturges v. Carter*, 114 U. S. 521, 5 Sup. Ct. 1014; *Bradley v. Bauder*, 36 Ohio St. 28.

and must be uniformly assessed. Corporations are persons within the protection of this rule.⁸⁴

If the state, in granting a charter, has stipulated that it will not tax the corporation, or that it will tax it in a certain way only, or on certain property only, or to a certain amount only, it cannot afterwards tax in violation of the stipulation, without violating the clause of the federal constitution, by which it is declared that no state shall pass any law impairing the obligation of contracts. This subject will be more fully explained on a subsequent page.⁸⁵

A state cannot tax United States government bonds. Therefore it cannot tax the capital of corporations—like national banks, for instance—which is invested in such bonds.

A state can impose no tax upon railroad or other corporations that amounts to a regulation of or interference with foreign or interstate commerce, for by the federal constitution the power to regulate commerce is vested exclusively in congress. Thus a state could not impose a tax upon freight or passengers transported by a railroad company into or through the state. A state law imposing a tax on freight or passengers, so far as it applies to articles or persons carried through the state, or taken up in the state and carried out of it, or taken up out of the state and brought into it, is unconstitutional and void.⁸⁶ But a state may tax a corporation on freight or passengers transported from point to point in the state. And a tax upon

⁸⁴ By section 4 of the thirteenth article of the constitution of California, "a mortgage, deed of trust, contract, or other obligation by which a debt is secured," is treated, "for the purposes of assessment and taxation, as an interest in the property affected thereby"; and, "except as to railroad and other quasi public corporations," the value of the property affected, less the value of the security, is to be assessed and taxed to its owner, and the value of the security is to be assessed and taxed to its holder. But by section 10 of the same article, "the franchise, roadway, roadbed, rails, and rolling stock of all railroads operated in more than one county" are to be assessed at their actual value, and apportioned to the counties, cities, and districts in which the roads are located, in proportion to the number of miles of railway laid therein; no deduction from this value being allowed for any mortgages on the property. It has been held that in the different modes thus prescribed of assessing the value of the property of natural persons and the property of railroad corporations, as the basis of taxation, there is a departure from the rule of equality and uniformity. *Railroad Tax Cases*, 13 Fed. 722.

⁸⁵ Post, p. 227.

⁸⁶ *State Freight Tax Case*, 15 Wall. 232; *Crandall v. Nevada*, 6 Wall. 35.

the gross receipts of a railroad company, after they have reached its treasury, is not an interference with interstate commerce, though part of the receipts may have been derived from transportation of persons or property into, out of, or through the state.⁸⁷ The same principles apply to telegraph companies and all other corporations engaged in interstate or foreign commerce.⁸⁸ The effect of the interstate commerce clause of the federal constitution on the power of the states to tax foreign corporations is considered in dealing with the law relating to foreign corporations.⁸⁹

Since the states have no power, by taxation or otherwise, to impede or in any manner control the operation of the constitutional laws enacted by congress to carry into effect the powers vested in the national government, it follows that, where congress creates a corporation as a means of executing a power conferred by the federal constitution,⁹⁰ the franchises of the corporation cannot be taxed by a state without the consent of congress.⁹¹ A state, however, may tax property owned by the corporation within its limits, and it may tax shares in the corporation against resident owners.⁹²

The states can exercise no control over national banks, nor in any way affect their operation, except in so far as congress may see fit to permit.⁹³ The franchises, therefore, of a national bank, could not be taxed by a state. Congress, in the national banking act, has expressly declared the shares in national banks to be taxable by the states against the holders as personal property,⁹⁴ provided "the taxa-

⁸⁷ *State Tax on Railway Gross Receipts*, 15 Wall. 284. But, if the tax is levied specifically upon the gross receipts for the carriage of freight or passengers into, out of, or through the state, it is void. *Fargo v. Michigan*, 121 U. S. 230, 7 Sup. Ct. 857; *Philadelphia & Southern S. S. Co. v. Pennsylvania*, 122 U. S. 326, 7 Sup. Ct. 1118.

⁸⁸ *Telegraph Co. v. Texas*, 105 U. S. 460.

⁸⁹ *Post*, p. 618.

⁹⁰ *Ante*, p. 39.

⁹¹ *McCulloch v. Maryland*, 4 Wheat. 316; *California v. Central Pac. R. Co.*, 127 U. S. 1, 8 Sup. Ct. 1073.

⁹² *McCulloch v. Maryland*, *supra*; *Railroad Co. v. Peniston*, 18 Wall. 5.

⁹³ *Farmers' & Mechanics' Nat. Bank v. Dearing*, 91 U. S. 29.

⁹⁴ This allows taxation of shares in national banks against other national banks which may hold them. *National Bank v. City of Boston*, 125 U. S. 60, 8 Sup. Ct. 772.

tion shall not be at a greater rate than is assessed upon other monied capital in the hands of individual citizens of such state,"⁹⁵ and provided shares owned by nonresidents shall be taxed where the bank is located. Real property of national banks is also declared taxable by the states. Capital of national banks invested in United States government bonds is, of course, not taxable.

Exemption from Taxation.

Some of the state constitutions expressly prohibit the legislature from granting exemptions from taxation, except to charitable institutions, and in certain other special cases. And some of the state courts have held, independently of any such prohibition, that the taxing power of the state is a power which the legislature cannot barter away, and that a grant of exemption from taxation is revocable.⁹⁷ But, according to the decisions of the supreme court of the United States, and the decisions of most of the state courts, in the absence of constitutional restrictions, a state may, in granting a charter, stipulate that the corporation shall be exempt from taxation, or that it shall be taxable only to a certain amount, or on certain property, or in a certain way; and if it does so in clear and unmistakable terms, it cannot afterwards impose a tax in violation of the charter, without impairing the obligation of its contract with the corporation, and so violating the federal constitution.⁹⁸

If an exemption of the property of a corporation from taxation,

⁹⁵ Rev. St. U. S. § 5219. As to the effect of this provision, see *People v. Weaver*, 100 U. S. 539; *Boyer v. Boyer*, 113 U. S. 689, 5 Sup. Ct. 706; *Mercantile Bank v. City of New York*, 121 U. S. 138, 7 Sup. Ct. 826; *Davenport Nat. Bank v. Board of Equalization*, 123 U. S. 83, 8 Sup. Ct. 73; *National Bank v. City of Boston*, 125 U. S. 60, 8 Sup. Ct. 772; *Whitbeck v. Bank*, 127 U. S. 193, 8 Sup. Ct. 1121.

⁹⁷ *Mechanics' & Traders' Branch of State Bank v. Debolt*, 1 Ohio St. 591; *Bank of Toledo v. City of Toledo*, Id. 622; *Skelly v. Bank*, 9 Ohio St. 606; *Mott v. Railroad Co.*, 30 Pa. St. 9. And see *West Wisconsin Ry. Co. v. Board of Sup'rs*, 35 Wis. 257.

⁹⁸ *Jefferson Branch Bank v. Skelly*, 1 Black, 436; *Home of the Friendless v. Rouse*, 8 Wall. 430; *Wilmington R. R. v. Reid*, 13 Wall. 264; *Dodge v. Woolsey*, 18 How. 331; *Farrington v. Tennessee*, 95 U. S. 679; *New Orleans v. Houston*, 119 U. S. 265, 7 Sup. Ct. 198; *Northwestern University v. People*, 99 U. S. 309; *Nichols v. Northampton Co.*, 42 Conn. 103; *Bank of Commerce v. McGowan*, 6 Lea (Tenn.) 703; *Mobile & O. R. Co. v. Moseley*, 52 Miss. 127; *Neustadt v. Railroad Co.*, 31 Ill. 484.

conceded by an act of the legislature, was spontaneous, and no service or duty or other condition was imposed upon the corporation, it may be revoked at the pleasure of the legislature, for there is no consideration.⁹⁹

It is well settled that exemption from taxation must be expressed in the charter in clear and unmistakable terms. An intention to grant exemption can never be implied from doubtful language. In this respect a charter will be strictly construed, and every doubt will be resolved in favor of the state and against the corporation.¹⁰⁰ For example, it has been held that an exemption of the capital stock of the corporation from taxation is not an exemption of property into which the capital stock has been converted.¹⁰¹ And a grant to one company of the powers and privileges of another, for the purpose of making and repairing a railroad, does not include an exemption from taxation, which was one of the privileges of the other company.¹⁰² And an exemption of the real estate of a charitable corporation from taxation cannot be construed as exempting it from an assessment for a local improvement.¹⁰³

If the legislature has reserved the power to repeal, alter, or amend the charter of a corporation, which it has exempted in whole or in part from taxation, the exemption is subject to revocation.¹⁰⁴ And, under such a reservation, if the charter fixes the taxes which the

⁹⁹ *Rector, etc., of Christ Church v. County of Philadelphia*, 24 How. 300; *Tucker v. Ferguson*, 22 Wall. 527; *Wilmington & W. R. Co. v. Alsbrook*, 110 N. C. 137; 14 S. E. 652, affirmed, 146 U. S. 279, 13 Sup. Ct. 72.

¹⁰⁰ *Delaware Railroad Tax*, 18 Wall. 206; *People v. Commissioners of Taxes*, 82 N. Y. 459, and cases cited in the following notes.

¹⁰¹ *Memphis & C. R. Co. v. Gaines*, 97 U. S. 697.

¹⁰² *Annapolis & Elk Ridge R. Co. v. Commissioners*, 103 U. S. 1; *Wilmington & W. R. Co. v. Alsbrook*, 110 N. C. 137, 14 S. E. 652, affirmed, 146 U. S. 279, 13 Sup. Ct. 72; *Philadelphia, W. & B. R. Co. v. Maryland*, 10 How. 376. Contra, *Nichols v. New Haven & Northampton Co.*, 42 Conn. 103. And compare *State Treasurer v. Auditor General*, 46 Mich. 224, 9 N. W. 258.

¹⁰³ *Roosevelt Hospital v. Mayor, etc., of City of New York*, 84 N. Y. 108.

¹⁰⁴ *Tomlinson v. Jessup*, 15 Wall. 454. And see *Nichols v. New Haven & Northampton Co.*, 42 Conn. 103; *Morris & E. R. Co. v. Commissioners of Railroad Taxation*, 37 N. J. Law, 228; *West Wisconsin Ry. Co. v. Board of Sup'rs of Trempealeau Co.*, 35 Wis. 257.

corporation shall be required to pay at a certain amount, they may be increased.¹⁰⁵

The cases do not agree as to what property of a corporation is exempt from taxation under a general exemption clause. There is no doubt that such a clause exempts all property that is reasonably necessary to carry out the objects for which the company was created.¹⁰⁶ It would also seem clear that such a clause exempts property which, though it might be dispensed with, is obviously appropriate and convenient for such purpose, for such property may well be said to be necessary.¹⁰⁷ It does not, however, exempt property which is not necessary, and which is not obviously appropriate and convenient, though it may be property which the corporation is authorized to hold.¹⁰⁸

¹⁰⁵ *Union Passenger Ry. Co. v. Philadelphia*, 101 U. S. 528.

¹⁰⁶ In *Lehigh Coal & Nav. Co. v. Northampton Co.*, 8 Watts & S. (Pa.) 334, it was held that, inasmuch as an incorporated canal was not taxable by the laws of Pennsylvania, not only the bed, berme bank, and tow path of the canal, but also the lock houses and collectors' offices, were exempt, as they were considered constituent parts of the canal, or necessarily incident thereto. And in *Railroad v. Berks Co.*, 6 Pa. St. 70, it was held that the exemption of a railroad covered water stations and depots, including the offices, oil houses, places to hold cars, etc., such places being necessary to the construction and operation of the road.

¹⁰⁷ In *Camden & A. Railroad & Transp. Co. v. Commissioners of Mansfield*, 23 N. J. Law, 510, it was said that property of a corporation is exempt from taxation, under a general exemption clause, only in so far as it is necessary, and not merely convenient, for the company to acquire and hold for the purposes for which it was incorporated; but in a later case it was held that this dictum was too narrow, and that the exemption includes whatever is obviously appropriate and convenient in carrying into effect the franchise granted. *New Jersey Railroad & Transp. Co. v. Hancock*, 35 N. J. Law, 545. And see *Illinois Cent. R. Co. v. Irvin*, 72 Ill. 456.

¹⁰⁸ In *Railroad Co. v. Berks Co.*, it was held that the exemption of a railroad from taxation, while it covered water stations, depots, offices, oil houses, places to hold cars, etc., did not include warehouses, coal lots, coal shutes, and wood yards, used or intended to be used as depots for merchandise, coal, wood, etc., for transportation, and machine shops for the manufacture of engines. In *Camden & A. Railroad & Transp. Co. v. Commissioners of Mansfield*, 23 N. J. Law, 510, it was held that exemption of a railroad company from taxation did not include dwelling houses and lots of land situated near the line of their road, and used exclusively by workmen and mechanics in the employ of the company. Compare *Northwestern University v. People*, 99 U. S. 309.

Where it is held that the property of stockholders in their shares, and the property of the corporation in its capital stock, are distinct property interests, a tax on shares of stock in the hands of the stockholders is not a tax on the capital of the corporation, in violation of an exemption. Thus the capital of national banks invested in United States securities is not taxable by the states, but shares of the stock in the hands of the individual stockholders may be taxed without deduction on account of such an investment.¹⁰⁹ So the franchises of a corporation may be taxed without deduction for a portion of its capital invested in government bonds.¹¹⁰ If a corporation is exempt from taxation, it cannot be taxed by a statute which purports to tax the shares of stockholders, but which requires the tax to be paid by the corporation, leaving it to collect the amount so paid from the stockholders, without regard to whether there may be any profits to be paid to the stockholders.¹¹¹

Ultra Vires.

The doctrine of ultra vires cannot be set up to defeat liability for taxes any more than it can be set up to defeat liability for torts, or to escape responsibility for a misdemeanor. A corporation cannot escape the taxes due upon its property or business on the ground that it was not authorized to acquire the property or to engage in the business.¹¹²

Foreign Corporations.

The right of a state to tax a foreign corporation doing business within its limits has nothing to do with the present subject,—the power of the state over corporations of its own creation,—and is considered in treating of foreign corporations in a subsequent chapter.¹¹³

¹⁰⁹ *Van Allen v. Assessors*, 3 Wall. 573; *National Bank v. Com.*, 9 Wall. 353.

¹¹⁰ *Manufacturers' Ins. Co. v. Loud*, 99 Mass. 146.

¹¹¹ *New Orleans v. Houston*, 119 U. S. 265, 7 Sup. Ct. 198.

¹¹² *Salt Lake City v. Hollister*, 118 U. S. 256, 6 Sup. Ct. 1055, 2 Cumming, Cas. Priv. Corp. 107.

¹¹³ Post, p. 612.

CHAPTER IX.

DISSOLUTION OF CORPORATIONS.

82. How Dissolution is Effected.

83-84. Equity Jurisdiction.

85. Effect of Dissolution.

HOW DISSOLUTION IS EFFECTED.

82. A private corporation may be dissolved in five ways:

- (a) By the weight of authority, by expiration of its charter.**
- (b) By an act of the legislature repealing its charter, under the power of repeal reserved by the state in granting the charter.**
- (c) By the loss of an essential integral part, which cannot be supplied; as by the death or withdrawal of all the members, where there are no means of supplying their places.**
- (d) By surrender of its charter with the consent of the state.**
- (e) By forfeiture of its charter for misuser or nonuser of its powers. But**
 - (1) A forfeiture only takes effect upon the judgment of a competent court ascertaining and decreeing a forfeiture, unless the legislature has clearly provided otherwise.**
 - (2) Where the acts or omissions of which the corporation has been guilty are, by statute, expressly made a cause of forfeiture, the court has no discretion to refuse a judgment of forfeiture. But in other cases the court has a discretion to determine from the circumstances whether judgment of ouster of the franchise to be a corporation shall be rendered, or**

whether the corporation shall be merely ousted from the exercise of the powers illegally assumed.

- (3) The legislature, as the representative of the state, may waive the right to insist upon a cause of forfeiture, as by acts recognizing the right of the body to continue as a corporation. But, to constitute a waiver, the acts must be inconsistent with the intention to insist upon a forfeiture.
- (4) The forfeiture must be enforced by the state, by its authorized representative. It cannot be enforced or insisted upon by private individuals, either collaterally or directly.
- (5) A forfeiture may be enforced by *scire facias* where there is a legal existing body, capable of acting, but who have abused their power; or by an information in the nature of *quo warranto* where the body is merely a corporation *de facto*, or where it is neither a corporation *de facto* nor *de jure*. The procedure is now generally fixed by statute.

These are the only ways mentioned in the books by which a corporation can cease to exist. It can be dissolved in no other way, except by express statutory provision.¹

Expiration of Charter.

According to the better opinion, and by the weight of authority, after the period of existence of a corporation has expired by force of express provision in its charter, or in a general law, it becomes *ipso facto* dissolved, and no longer has any existence at all, either *de jure* or *de facto*, for there is no law under which it can longer exist.²

¹ *Folger v. Insurance Co.*, 99 Mass. 267; *Morley v. Thayer*, 3 Fed. 737, 748.

² *Bradley v. Reppell* (Mo.) 32 S. W. 645; *Grand Rapids Bridge Co. v. Prange*, 35 Mich. 400; *Sturges v. Vanderbilt*, 73 N. Y. 384; *Dobson v. Simonton*, 86 N. C. 492; *Krutz v. Town Co.*, 20 Kan. 397; *La Grange & M. R. Co. v. Rainey*, 7 Cald. (Tenn.) 432; 2 Mor. Corp. § 1006.

Some courts hold, contrary to this proposition, that the fact that the charter of a corporation has expired does not terminate its existence, so as to prevent it from doing business, and suing and being sued; that it remains a *de facto* corporation, and subject to all the rules relating to such bodies, including the rule that its existence and right to do business can only be questioned by the state in a direct proceeding.³

Dissolution by Act of the Legislature.

As shown in a former chapter, the British parliament is, in theory at least, omnipotent, there being no constitutional restraints upon its action; and in England, therefore, corporations hold their charters at the will of the legislature. But in this country the power of the state legislatures and of congress is greatly restricted by constitutional provisions, the chief one of which, as far as the present subject is concerned, is the provision contained in the federal constitution, and also in most of the state constitutions, that no state shall pass any law impairing the obligation of contracts. The charter of a corporation; as we have seen, is a contract between the state and the corporators, and the state cannot dissolve a corporation which it has created, without the consent of the corporators,⁴ unless it has reserved the right to do so, or unless the corporation has been guilty of such an abuse of its franchises as to forfeit its charter. And even in the latter case, as we shall see, the forfeiture must generally be judicially ascertained and declared.⁵ Whether the state has reserved the right to repeal a charter, and thereby dissolve the corporation, is to be determined from the terms of the charter, and of such statutes as apply to the corporation, and so form a part of its charter. A corporation is dissolved and ceases to exist for any purpose as a body corporate upon the repeal of its charter by the legislature, by virtue of a power reserved in creating it.⁶ And a corporation is dissolved by a repeal of its charter, where there is no reserva-

³ *Miller v. Coal Co.*, 31 W. Va. 836, 8 S. E. 600; *Bushnell v. Machine Co.*, 138 Ill. 67, 27 N. E. 596.

⁴ *Ante*, p. 201.

⁵ *Post*, p. 237.

⁶ *Thornton v. Railway Co.*, 123 Mass. 32, 1 Cumming, Cas. Priv. Corp. 462, W. D. Smith, Cas. Corp. 167, *Shep. Cas. Corp.* 246; *Creasep v. Babcock*, 23 Pick. (Mass.) 334.

tion of power to repeal, if it accepts the repeal.⁷ This, however, is a surrender of its charter with the consent of the legislature.⁸

Loss of Integral Part—Death or Loss of Members.

"A corporation," said Chancellor Kent, "may also be dissolved when an integral part of the corporation is gone, without whose existence the functions of the corporation cannot be exercised, and when the corporation has no means of supplying that integral part, and has become incapable of acting. The incorporation becomes then virtually dead or extinguished."⁹ If all the members of a corporation should die or withdraw, and there were no way in which new members could come in, dissolution would necessarily result. To work a dissolution because of the loss of an integral part of the corporation, there must be a permanent incapacity to restore the part.¹⁰ Thus it has been held that dissolution does not result from an omission to continue the succession to certain offices, which are essential to the existence of the corporation, where the offices are in fact exercised by officers de facto, or even where there are no officers at all, if it is possible for the offices to be filled by an election or otherwise.¹¹ The statement that a corporation is dissolved by the death of all its members can have no application to modern business corporations, since the shares, being property, pass by assignment, bequest, or descent, and must ever remain the property of some persons, who must, of necessity, be members of the corporation as long as it may exist.¹²

Where a corporation is legally organized by the requisite number of persons, the fact that one person becomes the owner of all the shares of stock does not dissolve the corporation. It is still a corporation aggregate, and the stock may be transferred, and so distributed again. The property of the corporation remains vested in it,

⁷ Port Gibson v. Moore, 13 Smedes & M. (Miss.) 157.

⁸ Post, p. 235.

⁹ 2 Kent, Comm. 308, 309; King v. Pasmore, 3 Term R. 199; Philips v. Wickham, 1 Paige (N. Y.) 590.

¹⁰ Lehigh Bridge Co. v. Lehigh Coal & Nav. Co., 4 Rawle (Pa.) 9.

¹¹ Lehigh Bridge Co. v. Lehigh Coal & Nav. Co., supra; Philips v. Wickham, 1 Paige (N. Y.) 590; Russell v. M'Lellan, 14 Pick. (Mass.) 63. And see In re Belton, 47 La. Ann. 1614, 18 South. 642.

¹² Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 1 Cumming, Cas. Priv. Corp. 478, W. D. Smith, Cas. Corp. 165, Shep. Cas. Corp. 244.

and suits on causes of action accruing in favor of or against it are brought by or against it as a corporation.¹³ It has been held that in such an event the operation of the charter is suspended until, by a transfer of part of the stock, other members come in;¹⁴ but this is very doubtful, to say the least.¹⁵

Surrender of Charter.

It has been said that a corporation may be dissolved by the voluntary surrender of its charter; but this statement is too broad. Such a surrender cannot work a dissolution without an acceptance of the surrender, or consent on the part of the state. As was said by Morton, J., in a Massachusetts case: "Charters are in many respects compacts between the government and the corporators. And, as the former cannot deprive the latter of their franchises in violation of the compact, so the latter cannot put an end to the compact without the consent of the former. It is equally obligatory on both parties. The surrender of a charter can only be made by some formal, solemn act of the corporation; and it will be of no avail until accepted by the government. There must be the same agreement of the parties to dissolve that there was to form the compact. It is the acceptance which gives efficacy to the surrender. The dissolution of a corporation, it is said, extinguishes all its debts. The power of dissolving itself by its own act would be a dangerous power, and one which cannot be supposed to exist."¹⁶

Where a statute authorizes a corporation to surrender its charter, and transfer its property, rights, etc., to another corporation, and provides that upon such surrender and transfer, and acceptance thereof by the other corporation, the said charter shall be vacated and annulled, such a surrender, transfer, and acceptance result in a dis-

¹³ Ante, p. 7; *Button v. Hoffman*, 61 Wis. 20, 20 N. W. 667, 1 Cumming, Cas. Priv. Corp. 38; *Wilde v. Jenkins*, 4 Paige (N. Y.) 481; *Louisville Banking Co. v. Eiseman*, 94 Ky. 83, 21 S. W. 531, 1049; *Swift v. Smith*, 65 Md. 428, 5 Atl. 534; *Russell v. McLellan*, 14 Pick. (Mass.) 63; *In re Belton*, 47 La. Ann. 1614, 18 South. 642.

¹⁴ *Swift v. Smith*, supra; *Louisville Banking Co. v. Eisenman*, supra.

¹⁵ Cases cited in note 7a, supra; *Russell v. McLellan*, 14 Pick. (Mass.) 70; *Newton Manuf'g Co. v. White*, 42 Ga. 148.

¹⁶ *Boston Glass Manufactory v. Langdon*, 24 Pick. (Mass.) 49, 1 Cumming, Cas. Priv. Corp. 478, W. D. Smith, Cas. Corp. 165, *Shep. Cas. Corp.* 244. And see *Mylrea v. Railway Co.* (Wis.) 67 N. W. 1138.

solution of the corporation, and it no longer exists as such for any purpose.¹⁷ A corporation is dissolved on a repeal of its charter, and an acceptance of the repeal by it.¹⁸

A corporation cannot dissolve itself, before the expiration of the period fixed by its charter, without the consent of all the shareholders, unless such dissolution is provided for in the charter.¹⁹

Loss or Surrender of Property.

The possession of property is not at all essential to corporate existence; and it follows, therefore, that the insolvency of a corporation, or the transfer or loss of all its property, cannot work a dissolution.²⁰ Of course, if a corporation, by an assignment of all its property, violates its charter, the state may enforce a forfeiture; but that is a different question.

Where a statute declares that the stockholders of a corporation shall be liable for all debts due and owing by it at the time of its dissolution, it has been held that it is sufficient dissolution within the meaning of the statute if a corporation becomes totally insolvent, and suspends its business.²¹ But such insolvency and suspension of business does not dissolve a corporation for other purposes. It is merely a quasi dissolution as respects creditors.²² For instance, it would not prevent a receiver of the corporation from maintaining an action in its name against a director or other person against whom the corporation has a right of action.²³

Abandonment of Franchises or Business.

The neglect of a corporation to exercise or use the franchises granted to it by its charter, or the abandonment of its franchises,

¹⁷ *Mumma v. Potomac Co.*, 8 Pet. 281, 1 Cumming, Cas. Priv. Corp. 459.

¹⁸ *Port Gibson v. Moore*, 13 Smedes & M. (Miss.) 157.

¹⁹ *Barton v. Association*, 114 Ind. 226, 16 N. E. 486.

²⁰ 2 Kent, Comm. 309, 310; *Boston Glass Manufactory v. Langdon*, 24 Pick. (Mass.) 49, 1 Cumming, Cas. Priv. Corp. 478; *W. D. Smith, Cas. Corp.* 165, *Shep. Cas. Corp.* 244; *Parker v. Hotel Co.* (Tenn.) 34 S. W. 209; *Reichwald v. Hotel Co.*, 106 Ill. 439; *In re Belton*, 47 La. Ann. 1614, 18 South. 642; *State v. Bank of Maryland*, 6 Gill & J. (Md.) 205.

²¹ *Slee v. Bloom*, 19 Johns. (N. Y.) 456; *Briggs v. Penniman*, 8 Cow. (N. Y.) 387.

²² *Bank of Niagara v. Johnson*, 8 Wend. (N. Y.) 656; *Bradt v. Benedict*, 17 N. Y. 99; *Barclay v. Talman*, 4 Edw. Ch. (N. Y.) 128, 129.

²³ *Bank of Niagara v. Johnson*, *supra*.

may be ground for proceedings by the state to enforce a forfeiture of its charter, but it does not, ipso facto, work a dissolution.²⁴ Thus, where a canal company was incorporated, and authorized to maintain a dam for the purpose of supplying its canal, it was held, in effect, that its abandonment of the canal did not of itself work a forfeiture of its charter, and a dissolution, so as to make the maintenance of the dam unlawful, as against third persons.²⁵

Forfeiture of Charter.

A corporation may forfeit its charter and right to corporate existence by an abuse or misuser of its powers and franchises, or by neglect or nonuser. But it is well settled that, as a general rule, the forfeiture can only take effect upon a judgment of a competent tribunal in a proceeding by the state to enforce the forfeiture.²⁶ Whatever neglect of duty or abuse of power a corporation may be guilty of, it does not, in the absence of express statutory or charter provision, by reason of that alone, lose its corporate existence. Until it has had a hearing before a competent tribunal, and a forfeiture has been judicially declared by judgment of ouster, it continues to be a corporation for all purposes. In *State v. Fourth New Hampshire Turnpike*,²⁷ the defendant corporation had neglected to make returns to the legislature of expenditures and profits, as it was re-

²⁴ *Heard v. Talbot*, 7 Gray (Mass.) 113, 1 Cumming, Cas. Priv. Corp. 482; *Morley v. Thayer*, 3 Fed. 737, 748; *Parker v. Hotel Co. (Tenn.)* 34 S. W. 209; *Russell v. M'Lellan*, 14 Pick. (Mass.) 63; *Bradt v. Benedict*, 17 N. Y. 93; *Mylrea v. Railway Co. (Wis.)* 67 N. W. 1138; *Jones v. Herald Co.*, 44 S. C. 526, 22 S. E. 731.

²⁵ *Heard v. Talbot*, supra.

²⁶ 2 Kent, Comm. 312; *State v. Real-Estate Bank*, 5 Ark. 595; *King v. Amery*, 2 Term R. 515; *Colchester v. Seaber*, 3 Burrows, 1866; *Smith's Case*, 4 Mod. 53; *State v. Fourth New Hampshire Turnpike*, 15 N. H. 162, 1 Cumming, Cas. Priv. Corp. 593; *Boston Glass Manufactory v. Langdon*, 24 Pick. (Mass.) 49, 1 Cumming, Cas. Priv. Corp. 478, *W. D. Smith, Cas. Corp.* 165, *Shep. Cas. Corp.* 244; *Heard v. Talbot*, 7 Gray (Mass.) 113, 1 Cumming, Cas. Priv. Corp. 482; *Baker v. Backus' Adm'r*, 32 Ill. 79; *John v. Bank*, 2 Blackf. (Ind.) 367, 20 Am. Dec. 119; *Receivers of Bank of Circleville v. Renick*, 15 Ohio, 322; *Trustees of Vernon Soc. v. Hills*, 6 Cow. (N. Y.) 23; *Crump v. Mining Co.*, 7 Grat. (Va.) 352; *Greenbrier Lumber Co. v. Ward*, 30 W. Va. 43, 3 S. E. 227; *Mylrea v. Railway Co. (Wis.)* 67 N. W. 1138.

²⁷ *State v. Fourth N. H. Turnpike*, 15 N. H. 162, 1 Cumming, Cas. Priv. Corp. 593.

quired by its charter to do under penalty of forfeiture, but no proceedings were taken to obtain a judgment of forfeiture and ouster. It was held that the charter was not forfeited merely by the neglect, but that the corporation continued to exist, so that the right to enforce a forfeiture could be waived by the state. A provision in a charter that the corporation shall do certain things—as that it shall make periodical returns to the legislature of its expenditures and profits—“under forfeiture of the privileges of the act in future,” does not absolutely determine the existence of the corporation on a violation thereof; but the meaning is that the forfeiture shall be proved in the regular, legal manner, and a judgment of forfeiture in proper proceedings by the state is necessary.²⁸

It is perfectly competent, however, for the legislature, in granting a charter, or by an authorized amendment of a charter, to provide that the corporation shall lose its corporate existence without the intervention of the courts by any omission of duty or violation of its charter or default as to limitations imposed, and whether the legislature intended to so provide in any case depends upon the construction of the language used. In *Brooklyn Steam Transit Co. v. City of Brooklyn*,²⁹ the act incorporating a street-railroad company provided that, unless it should be organized, and should lay at least a certain amount of its road within a given time, “this act, and all the powers, rights, and franchises herein and hereby granted, shall be deemed forfeited and terminated.” The company organized, and made preparations to build its road, but did not build any portion of it before the expiration of the time limited, when it began to lay foundations for its road in the streets. It was held that under the provisions of the act it had lost its corporate franchises, and the right to build the road, and that the city could prevent it from proceeding with the work.³⁰

Same—When a Forfeiture will be Decreed.

Where a corporation has been guilty of acts or omissions which, by statute, are expressly made a cause of forfeiture of its franchise to be a corporation, the court, in proceedings by the state to en-

²⁸ *State v. Fourth N. H. Turnpike*, 15 N. H. 162, 1 Cumming, Cas. Priv. Corp. 593.

²⁹ *Brooklyn Steam Transit Co. v. City of Brooklyn*, 78 N. Y. 524.

³⁰ And see *In re Brooklyn, W. & N. Ry. Co.*, 72 N. Y. 245.

force such forfeiture, has no discretion to refuse a judgment.³¹ But in other cases the court is vested with discretion to determine whether judgment of ouster of the franchise to be a corporation shall be rendered, or whether the corporation shall be merely ousted from the exercise of the powers illegally assumed.³² In arriving at a determination of this question, the court will take into consideration, not only the interests of the public, but also the interests of the stockholders, and of creditors; and the extent to which corporate powers have been exceeded, the character of the acts done, etc., will be considered. Thus, though a building and loan association had been guilty of direct and repeated violations of its charter, the court, with some hesitation, however, gave judgment of ouster merely from the exercise of the powers illegally assumed, as it appeared that the corporation, if permitted, could wind up its affairs in a few months, and if it should be dissolved, it would be necessary to appoint trustees to wind it up under the statute, which would occasion delay, and involve increased expense.³³ One of the judges dissented on the ground that the violations of its charter were so flagrant and persistent as to call for the severest penalties of the law, and he was in favor of a judgment of ouster from the franchise of being a corporation. "To justify forfeiture of corporate existence," said Judge Finch in a late New York case, "the state, as prosecutor, must show on the part of the corporation accused some sin against the law of its being which has produced, or tends to produce, injury to the public. The transgression must not be merely formal or incidental, but material and serious, and such as to harm or menace the public welfare; for the state does not concern itself with the quarrels of private litigants. It furnishes for them sufficient courts and remedies, but intervenes as a party only where some public interest requires its action."³⁴

³¹ *State v. Pennsylvania & Ohio Canal Co.*, 23 Ohio St. 121; *State v. Oberlin Building & Loan Ass'n*, 35 Ohio St. 258, 1 Cumming, Cas. Priv. Corp. 566.

³² *State v. Oberlin Building & Loan Ass'n*, *supra*.

³³ *State v. Oberlin Building & Loan Ass'n*, *supra*.

³⁴ *People v. North River Sugar-Refining Co.*, 121 N. Y. 582, 24 N. E. 834, 1 Cumming, Cas. Priv. Corp. 570. So, in *State v. Minnesota Thresher Manuf'g Co.*, 40 Minn. 213, 41 N. W. 1020, it was held that the object of proceedings by quo warranto is to protect public interests, and therefore, to warrant a forfeiture of corporate franchises for misuser, the misuser must be such as to work or

Where a corporation enters into a partnership or association of independent corporations through the medium of a trust, for the purpose of obtaining a monopoly, disregarding all the statutory restraints as to the consolidation of corporations, and the rules of law prohibiting combinations in restraint of trade, it is guilty of such a violation of its charter, and such failure to perform its corporate duties, as renders it liable to dissolution in proceedings by the state.⁸⁵

Continued suspension of corporate franchises, and a failure to perform the implied conditions upon which the charter was granted, amount to a nonsuer, for which the charter may be forfeited.⁸⁶ But neither a mere temporary suspension of operations, nor an assignment for the benefit of creditors, is alone sufficient ground for forfeiture.⁸⁷

Where a penalty is fixed by the charter or statute under which a corporation is organized for the omission or commission of a par-

threaten a substantial injury to the public. In the syllabus by the court it is said: "Acts ultra vires, or in excess of powers, are not necessarily a misuser of franchises, such as will warrant their forfeiture. To justify such forfeiture, the ultra vires acts must be so substantial and continued as to so derange or destroy the business of the corporation that it no longer fulfills the end for which it was created. Ultra vires acts may be such as to justify interference by the state by injunction to prevent a continuance of the excess of powers, while they would not be a sufficient ground for a forfeiture of the corporate franchises in proceedings by quo warranto. If the unauthorized acts affect merely stockholders and creditors who have an adequate legal remedy, the state will not interfere." If an insurance company makes contracts of insurance, and accepts premiums, when it is in such a condition that there is no probability of its ever being able to pay losses, it is guilty of such an abuse of its franchises, as affords ground for forfeiture. *Ward v. Farwell*, 97 Ill. 593. For another instance of abuses held ground for forfeiture, see *Bank of Vincennes v. State*, 1 Blackf. (Ind.) 267.

⁸⁵ *People v. North River Sugar-Refining Co.*, supra. And see *State v. Nebraska Distilling Co.*, 29 Neb. 700, 46 N. W. 155; *Distilling & Cattle Feeding Co. v. People*, 156 Ill. 448, 41 N. E. 188; *State v. Standard Oil Co.*, 49 Ohio St. 137, 30 N. E. 279; *People v. Chicago Gas Trust Co.*, 130 Ill. 268, 22 N. E. 798. But see *U. S. v. E. C. Knight Co.*, 156 U. S. 1, 15 Sup. Ct. 249.

⁸⁶ *State v. Commercial Bank of Manchester*, 13 Smedes & M. (Miss.) 569; *State v. Real-Estate Bank*, 5 Ark. 595. As where a railroad company, without authority of law, leases its road to another company, with all its rights, property, and franchises, for a long period of time, and abandons the operation of its road. *State v. Atchison & N. R. Co.*, 24 Neb. 143, 38 N. W. 43.

⁸⁷ *State v. Commercial Bank of Manchester*, supra.

ticular act, the penalty prescribed is generally the only punishment that can be inflicted for doing or omitting to do the act. It is no ground for forfeiture, the presumption being that the legislature intended the penalty as satisfaction for the breach.³⁸

If a corporation has not complied with the law in its organization, so that, though it is a corporation de facto, it is not a corporation de jure, the remedy is by quo warranto by the state. Private individuals, as we have seen, cannot attack the existence of the corporation, or question its right to do business.³⁹ In quo warranto by the state, however, its charter will be forfeited. Thus, where the state, by quo warranto proceedings, directly challenged the right of certain persons to act as a railway corporation, and it appeared that many of the subscribers for the stock were notoriously insolvent, and had no expectation, at the time they subscribed, of ever paying their subscription, thus leaving the amount subscribed in good faith less than that required by the statute, it was held that a judgment of forfeiture was proper.⁴⁰ So, where a corporation is illegally formed by a trust combination for the purpose of obtaining a monopoly in the manufacture and sale of an article, and controlling the production, and the price, quo warranto will lie.⁴¹

Same—Waiver of Forfeiture.

It is well settled that the state may waive the right to insist upon a forfeiture of the charter of a corporation because of a violation thereof, just as one individual may waive the right to object to the breach of a term of his contract with another. And such a waiver is generally established by showing that the legislature, with knowledge of the ground of forfeiture, recognized the continued existence and right to existence of the corporation.⁴² Thus, where the charter of a turnpike corporation required it to make returns to the legislature, every sixth year, of its expenditures and profits, under pen-

³⁸ State v. Real-Estate Bank, 5 Ark. 595.

³⁹ Ante, p. 86.

⁴⁰ Holman v. State, 105 Ind. 569, 5 N. E. 702.

⁴¹ Distilling & Cattle Feeding Co. v. People, 156 Ill. 448, 41 N. E. 188. See ante, p. 71.

⁴² State v. Real-Estate Bank, 5 Ark. 595; State v. Fourth New Hampshire Turnpike, 15 N. H. 162, 1 Cumming, Cas. Priv. Corp. 593; State v. Bailey, 19 Ind. 452; Mylrea v. Railway Co. (Wis.) 67 N. W. 1138.

alty of forfeiture, and the corporation failed to make such returns for over twenty years, it was held that the legislature, by accepting and acquiescing in returns made after such violation of the charter, and also by passing an act authorizing the corporation to change its route, waived any right it may have had to insist upon a forfeiture.⁴³ The doctrine of waiver of a forfeiture by the state by subsequent legislative acts does not apply where, by the terms of the charter, the franchise absolutely determines upon failure to perform certain conditions.⁴⁴

If the acts relied upon as a waiver of a cause of forfeiture are perfectly consistent with the intention to insist upon a forfeiture, they will not be regarded as a waiver. Thus where a corporation had violated its charter by taking usury, it was held by the New York court that, even conceding that the governor and senate could waive a forfeiture, the right to insist upon a forfeiture was not waived by the act of the governor and senate in appointing a state director of the corporation. "Notwithstanding the existing cause of forfeiture," it was said, "the defendants were a corporation de facto, and might continue to exercise their franchise until judgment of ouster should be pronounced against them. In the meantime it was the duty of the governor and senate, as well as all others, to treat the defendants as a legally existing corporation. The appointment of a state director was, therefore, perfectly consistent with the intention to continue this prosecution, and insist on the forfeiture."⁴⁵

The right to insist upon a forfeiture can be waived only by the legislature, legally acting as such. Neither the attorney general, nor the governor, nor the state senate alone, nor any other man or body of men, save only the legislature, has this power.⁴⁶

Same—The State Only can Enforce Forfeiture.

Proceedings to forfeit the charter of a corporation must be brought directly by the state, or by its authorized representative acting in its name. As a general rule, no advantage can be taken of the misuser or nonuser of its powers and franchises by a corporation, or of

⁴³ State v. Fourth New Hampshire Turnpike, *supra*.

⁴⁴ State v. Fourth New Hampshire Turnpike, *supra*.

⁴⁵ People v. Phoenix Bank, 24 Wend. (N. Y.) 431, 1 Cumming, Cas. Priv. Corp. 597.

⁴⁶ People v. Phoenix Bank, *supra*.

failure to comply with conditions subsequent in its charter, by private individuals, either collaterally or directly.⁴⁷ In *Heard v. Talbot*,⁴⁸ a canal company, which was authorized to maintain a dam for the purpose of supplying its canal with water, abandoned the use of the canal. Private individuals afterwards brought suit for the flowing of their land by reason of the maintenance of the dam, and contended that the abandonment of the canal worked a forfeiture of the right to maintain the dam, and that its maintenance was, therefore, unlawful. The court held, however, that the abandonment of the canal was merely a violation of its charter by the corporation, and, while it might be cause for forfeiture in proceedings by the state to enforce a forfeiture, it could not thus be taken advantage of collaterally by private individuals.⁴⁹

⁴⁷ 2 Kent, Comm. 312; *Heard v. Talbot*, 7 Gray (Mass.) 113, 1 Cumming, Cas. Priv. Corp. 482; *Com. v. Union F. & M. Ins. Co.*, 5 Mass. 230; *Baker v. Backus' Adm'r*, 32 Ill. 79; *Toledo & A. A. R. Co. v. Johnson*, 49 Mich. 148, 13 N. W. 492; *Trustees of Vernon Soc. v. Hills*, 6 Cow. (N. Y.) 23; *Crump v. Mining Co.*, 7 Grat. (Va.) 352; *John v. Bank*, 2 Blackf. (Ind.) 367; *Boston Glass Manufactory v. Langdon*, 24 Pick. (Mass.) 49, 1 Cumming, Cas. Priv. Corp. 478, *W. D. Smith, Cas. Corp.* 165, *Shep. Cas. Corp.* 244; *Greenbrier Lumber Co. v. Ward*, 30 W. Va. 43, 3 S. E. 227; *Bank of Circleville v. Renick*, 15 Ohio, 322. Contra, by statute, *State v. Webb*, 97 Ala. 111, 12 South. 377.

⁴⁸ 7 Gray (Mass.) 113, 1 Cumming, Cas. Priv. Corp. 482.

⁴⁹ The court said in this case: "Although the disuse of the canal and its abandonment by the corporation may be a gross disregard of the duty imposed on them by law, and an essential violation of the terms and conditions implied from the contract entered into with the government by the acceptance of the charter, and upon due proceedings had, might be a sufficient ground upon which to decree a forfeiture of all their corporate rights and privileges, they do not constitute any valid ground upon which the exercise by the corporation of any of the powers conferred by their charter can be defeated or denied by third persons in collateral proceedings. This results from the very nature of an act of incorporation. It is not a contract between the corporate body, on the one hand, and individuals whose rights and interests may be affected by the exercise of its powers, on the other. It is a compact between the corporation and the government from which they derive their powers. Individuals, therefore, cannot take it upon themselves, in the assertion of private rights, to insist on breaches of the contract by the corporation, as a ground for resisting or denying the exercise of a corporate power. That can be done only by the government with which the contract was made, and in proceedings duly instituted against the corporation. It would not only be a great anomaly to allow persons, not parties to the contract, to insist on its breach, and enforce a penalty for its violation;

Nor can private individuals institute direct proceedings to enforce a forfeiture of a charter. An information in the nature of quo warranto may be granted to inquire into the election or admission of an officer or member of a corporation, when moved for by any person interested in or injured by such election or admission. But private persons cannot move for such an information in order to obtain a judgment of forfeiture of the charter of a corporation. Such an information can be prosecuted only by the authority of the state, acting by its proper officers.⁵⁰ This necessarily results from the doctrine that the state may waive a forfeiture.

Same—Modes of Proceeding to Enforce Forfeiture.

There are at common law two modes of proceeding judicially to ascertain and enforce the forfeiture of a charter for misuser or non-user.⁵¹ One is by scire facias; and that process is proper where there is a legal existing body, capable of acting, but which has abused its power. The other mode is by information in the nature of a quo warranto, which is in form a criminal, and in its nature a civil, remedy; and that proceeding applies where there is a body corporate de facto only, but which takes upon itself to act, though, from some defect in its constitution, it cannot legally exercise its powers, or where an association assumes to act as a corporation without even color of authority. Both of these modes of proceeding against corporations are at the instance and on behalf of the state. Private individuals, as we have seen, cannot institute proceedings, unless there is some statute expressly allowing them to do so. The judgment in such proceedings is that the parties be ousted from the exercise of corporate powers and privileges. The mode of proceeding is now very generally prescribed and regulated by statute, and in most states information in the nature of quo warranto is the mode in all cases.

but it would be against public policy, and lead to confusion of rights, if corporate powers and privileges could be disputed and defeated by every person who might be aggrieved by their exercise. Therefore, it has been often held that a cause of forfeiture, however great, cannot be taken advantage of or enforced against corporations collaterally or incidentally, or in any other mode than by a direct proceeding for that object in behalf of the government."

⁵⁰ *Com. v. Union Fire & Marine Ins. Co.*, 5 Mass. 230, 1 Cumming, Cas. Priv. Corp. 599.

⁵¹ 2 Kent, Comm. 313, 314.

THE JUDICIAL POWER

83. A court is not to be regarded as having jurisdiction of a case until it has taken jurisdiction of the parties to the suit. It is not enough that the parties are within the jurisdiction of the court at the time the suit is brought. The parties must be brought within the jurisdiction of the court by the court's process.

84. The jurisdiction of a court is not to be regarded as having been acquired until the court has taken jurisdiction of the parties to the suit. It is not enough that the parties are within the jurisdiction of the court at the time the suit is brought. The parties must be brought within the jurisdiction of the court by the court's process. The jurisdiction of a court is not to be regarded as having been acquired until the court has taken jurisdiction of the parties to the suit. It is not enough that the parties are within the jurisdiction of the court at the time the suit is brought. The parties must be brought within the jurisdiction of the court by the court's process.

As to the jurisdiction of a court to hear a case.

The court has jurisdiction of a case if the parties to the suit are within the jurisdiction of the court at the time the suit is brought. It is not enough that the parties are within the jurisdiction of the court at the time the suit is brought. The parties must be brought within the jurisdiction of the court by the court's process. The jurisdiction of a court is not to be regarded as having been acquired until the court has taken jurisdiction of the parties to the suit. It is not enough that the parties are within the jurisdiction of the court at the time the suit is brought. The parties must be brought within the jurisdiction of the court by the court's process.

⁸² Post, p. 380.

⁸³ Strong v. McCagg, 55 Wm. 624, 13 N. W. 835; Haden v. Newton, 14 Blatch. 376, Fed. Cas. No. 6054, 1 Cumming. Cas. Rep. 487; Haden v. Screw Co., 3 R. L. 9; Verplanck v. Insurance Co., 1 Edw. Ch. (N. Y.) 84; Haden v. Oure, 1 Freem. Ch. (Miss.) 161; State v. Merchants' Insurance & Loan Co., 8 Humph. (Tenn.) 235; Com. v. Union Fire & Marine Ins. Co., 5 Mass. 281; Folger v. Insurance Co., 99 Mass. 274; Neall v. Hill, 16 Cal. 145; Howe v. Deuel, 43 Barb. (N. Y.) 504; Waterbury v. Express Co., 50 Barb. 157; Holmont v. Railway Co., 52 Barb. 637; Denike v. Cement Co., 80 N. Y. 504.

times expressly conferred by statute under particular circumstances. Without this, it does not exist. "General jurisdiction of writs against corporations no more implies a power to destroy a corporation at the suit of an individual than jurisdiction of private suits against individuals authorizes the court to entertain a prosecution for crime, to pass sentence of death, and to issue a warrant for execution. The only modes of dissolving a corporation known to the common law were by the death of all its members; by act of the legislature; by a surrender of the charter, accepted by the government; or by forfeiture of the franchise, which could only take effect upon a judgment of a competent tribunal on a proceeding in behalf of the state; and neither a court of law nor a court of equity had jurisdiction to decree a forfeiture of the charter or dissolution of the corporation at the suit of an individual."⁵⁴ When by statute a court of equity is given such jurisdiction under particular circumstances, it can only interfere when the case comes within the statute.⁵⁵

This doctrine has been held subject to exceptions. In a late Michigan case⁵⁶ it was said: "The general rule undoubtedly is that courts of equity have no power to wind up a corporation, in the absence of statutory authority. This rule is, however, subject to qualifications. It has been held that when it turns out that the purposes for which a corporation was formed cannot be attained it is the duty of the company to wind up its affairs; that the ultimate object of every ordinary trading corporation is the pecuniary gain of its stockholders; that it is for this purpose, and no other, that the capital has been advanced; and, if circumstances have rendered it impossible to continue to carry out the purpose for which it was formed with profit to its stockholders, it is the duty of its managing agents to wind up its affairs. To continue the business of the company under such circumstances would involve both an unauthorized exercise of corporate franchises and a breach of the charter contract." And it was held that in a suit by a stockholder against the corporation, its directors, and other stockholders, for an accounting and the appointment of a receiver to wind up the affairs of the company, where it appeared that the defendants owned a majority of the

⁵⁴ *Folger v. Insurance Co.*, *supra*.

⁵⁵ *Hardon v. Newton*, *supra*.

⁵⁶ *Miner v. Ice Co.*, 93 Mich. 97, 53 N. W. 218, 2 Cumming, *Case Priv. Corp.* 234.

stock, and had for a number of years controlled the corporation in their own interest, and for their own profit, fraudulently excluding the complainant, and paying no dividends to him, the failure to pay being due to their fraud, and not to natural causes, the court had jurisdiction to wind up the corporation, and distribute its assets. "This corporation," it was said, "has utterly failed of its purpose, not because of matters beyond its control, but because of fraudulent mismanagement and misappropriation of its funds. Complainant has a right to insist that it shall not continue as a cloak for a fraud upon him, and shall not longer retain his capital to be used for the sole advantage of the owner of the majority of the stock; and a court of equity will not so far tolerate such a manifest violation of the rules of natural justice as to deny him the relief to which his situation entitles him. I think a court of equity, under the circumstances of this case, in the exercise of its general equity jurisdiction, has the power to grant to this complainant ample relief, even to the dissolution of the trust relations."

At the Suit of the State.

A court of equity has no inherent jurisdiction to forfeit the charter of a corporation, or decree a dissolution, at the suit of the state. A court of equity does not administer punishment or enforce forfeitures for transgressions of law, but is limited in its jurisdiction to the protection of civil rights, and it is also limited in its jurisdiction to cases in which there is no adequate remedy at law. An information, therefore, cannot be maintained in equity in the name of the state or the attorney general to forfeit the charter of a corporation for misuse or nonuser, or to enjoin a corporation or pretended corporation from exercising unauthorized powers, unless, in the latter case, there is some peculiar ground for equitable interference; but the only remedy is at law by quo warranto or scire facias.⁵⁷

A court of equity, however, has jurisdiction to grant relief by injunction in two cases: (1) Where the acts complained of constitute or threaten a public nuisance, which affects or endangers the public safety or convenience, and requires immediate judicial interposition,

⁵⁷ Attorney General v. Tudor Ice Co., 104 Mass. 239, 1 Cumming, Cas. Priv. Corp. 585; Attorney General v. Utica Ins. Co., 2 Johns. Ch. (N. Y.) 371; Attorney General v. Stevens, 1 N. J. Eq. 369. Contra, Chicago Fair Grounds Ass'n v. People, 60 Ill. App. 488.

like obstruction of highways and navigable rivers;⁵⁸ and (2) where there is a charitable trust, and the beneficiaries are so numerous and indefinite that the breach of trust cannot be effectively redressed except by suit in equity in behalf of the public.⁵⁹

EFFECT OF DISSOLUTION.

85. When a corporation is dissolved, it is dead, and, in the absence of a statute to the contrary, it no longer exists for any purpose. Therefore, after dissolution,

(a) It can exercise no power, the right to exercise which depended upon its charter.

(b) It cannot be sued, nor can a suit previously commenced be prosecuted to judgement, nor can it sue.

(c) At common law.

(1) Debts due to or from it were extinguished.

(2) Real property undisposed of at the time of the dissolution reverted to the grantors or their heirs.

(3) Personal property owned by it at the time of dissolution escheated to the state.

(d) But a court of equity, under its general jurisdiction to enforce and administer trusts, has jurisdiction to avoid the effect of the common law to the extent of causing the debts due a dissolved corporation to be collected, and taking control of the corporate property and distributing it, so as to protect the equitable interests of creditors and shareholders.

(e) In most states, if not in all, there are now statutory provisions under which the business of dissolved

⁵⁸ *Attorney General v. Jamaica Pond Aqueduct Corp.*, 133 Mass. 361, 1 Cumming, Cas. Priv. Corp. 589; *Attorney General v. Great Northern Ry. Co.*, 4 De Gex & S. 75.

⁵⁹ *Attorney General v. Garrison*, 101 Mass. 223; *Jackson v. Phillips*, 14 Allen (Mass.) 539; *Parker v. May*, 5 Cush. (Mass.) 336.

corporations may be liquidated and settled, and the equities of shareholders and creditors may be enforced

When the charter of a corporation is repealed, or the corporation is otherwise dissolved, the corporation or members can no longer exercise any powers the right to exercise which depended upon the charter. If the corporation be a bank, for instance, authorized to lend money and issue circulating notes, it cannot make new loans or issue new notes. If the corporation was chartered to operate a railroad, and authorized to use the streets of a city for that purpose, it can no longer use the streets or exercise the franchise of running a railroad in the city. In short, whatever power is dependent solely upon the grant of the charter, and which could not be exercised by unincorporated private persons, under the general laws of the state, is abrogated by the repeal of the law which granted these special rights.⁶⁰

When a corporation has been legally dissolved, it is no longer in existence for any purpose. It is dead. It cannot be recognized for the purpose of proceedings by or against it any more than could a dead natural person. Thus scire facias to revive a judgment recovered against a corporation cannot be maintained against it, and a judgment had thereon, after the corporation has been legally dissolved.⁶¹ Nor can an action be maintained against it, or an action previously commenced be prosecuted to judgment. A judgment rendered against a corporation after it has been legally dissolved is as wholly void as if it had been rendered against a dead person.⁶² Nor can an action be brought by or in the name of a corporation after its dissolution.⁶³

⁶⁰ *Greenwood v. Freight Co.*, 105 U. S. 13; 1 Cumming, Cas. Priv. Corp. 538; W. D. Smith, Cas. Corp. 160; Shep. Cas. Corp. 260.

⁶¹ *Mumma v. Potomac Co.*, 8 Pet. 281, 1 Cumming, Cas. Priv. Corp. 459.

⁶² *Thornton v. Railway Co.*, 123 Mass. 82, 1 Cumming, Cas. Priv. Corp. 462, W. D. Smith, Cas. Corp. 167, Shep. Cas. Corp. 246; *Sturges v. Vanderbilt*, 73 N. Y. 384; *Dobson v. Simonton*, 86 N. C. 492; *Krutz v. Town Co.*, 20 Kan. 397. As to whether expiration of charter ipso facto amounts to a dissolution, within this rule, see ante, p. 282.

⁶³ *Boston Glass Manufactory v. Langdon*, 24 Pick. (Mass.) 49, 1 Cumming, Cas. Priv. Corp. 478, W. D. Smith, Cas. Corp. 165, Shep. Cas. Corp. 244.

Chancellor Kent said: "According to the old settled law of the land, where there is no special statute provision to the contrary, upon the civil death of a corporation, all its real estate remaining unsold reverts back to the original grantor and his heirs. The debts due to and from the corporation are all extinguished. Neither the stockholders nor the directors or trustees of the corporation can recover those debts, or be charged with them, in their natural capacity. All the personal estate of the corporation vests in the people, as succeeding to this right and prerogative of the crown at common law."⁶⁴

Such were the common-law rules,⁶⁵ but, as respects private business corporations, they are now obsolete. They were established before modern trading and commercial corporations came into existence. With the growth of such corporations, the legislatures and the courts have been obliged to abolish or change many of the common-law rules,—these among others. These rules have not been recognized in equity. While a private corporation holds the legal title to the corporate property as a distinct legal person, it holds it in equity merely for the benefit of the stockholders and of creditors. If the corporation is dissolved, and ceases to exist, the debtors of the corporation are not, in equity, released from their liability, the creditors of the corporation are not left without a remedy to recover the amount due them, and the property of the corporation does not revert to the grantors, or escheat to the state, instead of belonging to the stockholders. It is true that the legal title to the property does not vest in the stockholders, but they still retain the beneficial interest therein; and, if the legislature has made no provision by which they can reach it, and enforce their rights, they may come into a court of equity, and obtain relief. Such a court has jurisdiction, unless it has been taken away by statute, to reach the property of the defunct corporation, to cause the debts due to it to be collected, and to distribute the assets, after payment of the creditors, to the beneficial owners, that is, to the members or stockholders.⁶⁶

⁶⁴ 2 Kent, Comm. 307; Co. Litt. 13b.

⁶⁵ 1 Bl. Comm. 484; 2 Kyd, Corp. 516; *Hightower v. Thornton*, 8 Ga. 486; *Port Gibson v. Moore*, 13 Smedes & M. (Miss.) 157; *State Bank v. State*, 1 Blackf. (Ind.) 267; *Fox v. Horah*, 1 Ired. Eq. (N. C.) 358.

⁶⁶ *Bacon v. Robertson*, 18 How. 480, 1 Cumming, Cas. Priv. Corp. 468; *High-*

There are now statutes in most states, if not in all, prescribing the mode by which the business of dissolved corporations may be liquidated and settled, and by which the equities of the creditors and members respectively may be enforced. In many states there are statutes by which corporations whose powers would expire by express limitation in their charters or otherwise are continued bodies corporate for a certain length of time from and after the day on which their powers would cease, for the purpose of prosecuting and defending suits, and of enabling them to gradually settle and close their business, and divide their capital stock, but not for the purpose of continuing business.⁶⁷ Such statutes are not invalid as impairing the obligation of contracts, nor are they invalid as being retrospective, because, as it generally the case, they are made applicable to corporations previously created, as well as to those created afterwards.⁶⁸

If a corporation, when it ceases to exist, has no members, and owes no debts, the common-law rule by which its property reverts or escheats applies. It has been held, for instance, that where a cor-

tower v. Thornton, 8 Ga. 486; Folger v. Insurance Co., 99 Mass. 267. When the charter of a corporation expires, the officers or trustees may safely distribute the assets to those who appear on the books of the company as stockholders, and need not require production of the stock certificates, "As between adverse claimants of the certificate, the possession of it, with the transfer upon it, is often the test of the title. But when the corporation itself is not dealing with its stockholder on the security of his stock, and is merely performing a corporate duty, its own record is all it needs to consult, for whoever would demand the privileges of a stockholder should produce the evidence of his title, and ask to be permitted to participate." Bank of Commerce's Appeal, 73 Pa. St. 59. The same is true of the payment of dividends. See post, p. 348. Where a corporation exists by law, after the expiration of its charter, solely for the purpose of winding up its affairs, a majority in interest of its stockholders cannot sell its property to a new corporation, of which they are directors and stockholders, at a valuation estimated by themselves, against the will of the minority, and compel such dissenting stockholders either to receive shares of stock in the new corporation in return for their old shares, or to be paid therefor on the basis of the estimated valuation of the property, and the minority may have the property publicly sold. Mason v. Mining Co., 133 U. S. 50, 10 Sup. Ct. 224, Shep. Cas. Corp. 215.

⁶⁷ Foster v. Bank, 16 Mass. 245, 1 Cumming, Cas. Priv. Corp. 464.

⁶⁸ Foster v. Bank, 16 Mass. 245, 1 Cumming, Cas. Priv. Corp. 464.

poration which, like a mutual insurance company, has no stockholders, ceases to exist, the last policy having expired, and there no longer being any members, the common-law rule, which gives its surplus assets to the state, still applies, and the assets do not go to the former policy holders, nor to the original corporators.⁶⁹

The common-law rule still applies to public and religious or charitable corporations. This question came up before the supreme court of the United States in a late case. Congress had repealed the charter granted by the territory of Utah, to the corporation known as the Church of Jesus Christ of Latter-Day Saints, and it was held that its property reverted and escheated to the United States, and that it made no difference that all the property was held in trust for the corporation by individuals.⁷⁰ "When a business corporation," it was said, "instituted for the purposes of gain or private interest, is dissolved, the modern doctrine is that its property, after payment of its debts, equitably belongs to its stockholders. But this doctrine has never been extended to public or charitable corporations. As to these, the ancient and established rule prevails, namely, that when a corporation is dissolved, its personal property, like that of a man dying without heirs, ceases to be the subject of private ownership, and becomes subject to the disposal of the sovereign authority; while its real estate reverts or escheats to the grantor or donor, unless some other course of devolution has been directed by positive law, though still subject, as we shall hereafter see, to the charitable use." The court held that, as the real estate of the corporation was acquired by it from the United States under the town-site act, it reverted to the United States, and that its personal property also vested in the United States, to be applied, under the cy-pres doctrine, either by the court, or by the direction of congress, to some kindred object, whereby the general purposes of religion and charity may be promoted.⁷¹

⁶⁹ *Titcomb v. Insurance Co.*, 79 Me. 315, 9 Atl. 732, 1 Cumming, Cas. Priv. Corp. 476.

⁷⁰ And see *Fox v. Horah*, 1 Ired. Eq. (N. C.) 358.

⁷¹ *Late Corporation of Church of Jesus Christ v. U. S.*, 136 U. S. 1, 10 Sup. Ct. 792.

CHAPTER X.

MEMBERSHIP IN CORPORATIONS.

- 86. How Membership is Acquired.
- 87-88. "Capital Stock" and "Capital."
- 89-90. Nature of Shares of Stock.
- 91. Certificates of Stock.
- 92. Subscriptions to Stock—Subscriptions after Incorporation.
- 93-97. Subscriptions Prior to Incorporation.
- 98. Who may Become Subscribers.
- 99. Form of Subscription—Statutory Formalities.
- 100. Mutual Consent.
- 101. Subscriptions Induced by Fraud.
- 102. Subscriptions under Mistake.
- 103. Subscription by Agent.
- 104-106. Agents to Receive Subscriptions.
- 107-109. Conditional Subscriptions.
- 110-112. Subscriptions upon Special Terms.
- 113. Conditional Delivery of Subscription.
- 114-115. Subscription of Entire Capital, and Distribution.
- 116. Payment of Deposit.
- 117. Delivery of Certificate.
- 118-121. Remedy of Corporation on Subscriptions.
- 122-125. Calls.
- 126. Assignment of Unpaid Subscription.
- 127-132. Release and Discharge of Subscriber.
- 133. Estoppel of Subscriber.

HOW MEMBERSHIP IS ACQUIRED.

- 86. Membership in a corporation is acquired by contract with the corporation.
 - (a) In nonstock corporations the mode of forming the contract of membership is regulated by the charter and by-laws.
 - (b) In stock corporations membership is determined by the ownership of one or more shares of the capital stock, which may be acquired

Nor can private individuals institute direct proceedings to enforce a forfeiture of a charter. An information in the nature of quo warranto may be granted to inquire into the election or admission of an officer or member of a corporation, when moved for by any person interested in or injured by such election or admission. But private persons cannot move for such an information in order to obtain a judgment of forfeiture of the charter of a corporation. Such an information can be prosecuted only by the authority of the state, acting by its proper officers.⁵⁰ This necessarily results from the doctrine that the state may waive a forfeiture.

Same—Modes of Proceeding to Enforce Forfeiture.

There are at common law two modes of proceeding judicially to ascertain and enforce the forfeiture of a charter for misuser or non-user.⁵¹ One is by scire facias; and that process is proper where there is a legal existing body, capable of acting, but which has abused its power. The other mode is by information in the nature of a quo warranto, which is in form a criminal, and in its nature a civil, remedy; and that proceeding applies where there is a body corporate de facto only, but which takes upon itself to act, though, from some defect in its constitution, it cannot legally exercise its powers, or where an association assumes to act as a corporation without even color of authority. Both of these modes of proceeding against corporations are at the instance and on behalf of the state. Private individuals, as we have seen, cannot institute proceedings, unless there is some statute expressly allowing them to do so. The judgment in such proceedings is that the parties be ousted from the exercise of corporate powers and privileges. The mode of proceeding is now very generally prescribed and regulated by statute, and in most states information in the nature of quo warranto is the mode in all cases.

but it would be against public policy, and lead to confusion of rights, if corporate powers and privileges could be disputed and defeated by every person who might be aggrieved by their exercise. Therefore, it has been often held that a cause of forfeiture, however great, cannot be taken advantage of or enforced against corporations collaterally or incidentally, or in any other mode than by a direct proceeding for that object in behalf of the government."

⁵⁰ Com. v. Union Fire & Marine Ins. Co., 5 Mass. 230, 1 Cumming, Cas. Priv. Corp. 599.

⁵¹ 2 Kent, Comm. 313, 314.

EQUITY JURISDICTION.

83. A court of equity has no jurisdiction, unless it is conferred, as in some jurisdictions, by statute, to dissolve a corporation, and distribute its assets, at the suit of a stockholder or any other private individual. Some exceptions to this rule have been recognized.

84. Nor, generally, has a court of equity any jurisdiction to enforce a forfeiture, or enjoin exercise of unauthorized privileges and powers, at the suit of the state; but it may entertain an information to enjoin acts which constitute a public nuisance, and which require immediate interference, and it may assume jurisdiction in case of a charitable trust where the beneficiaries are numerous and indefinite, and the breach of trust cannot be effectively redressed except by suit in behalf of the public.

At the Suit of Private Individuals.

We shall see in a subsequent chapter that under certain circumstances a court of equity has jurisdiction to control and regulate the management of corporations at the suit of individual stockholders, where its interference is necessary to protect their equitable rights.⁵² But a very different question is presented when a stockholder or any other private individual, comes into a court of equity, and asks to have a corporation dissolved, and its assets distributed; and by the overwhelming weight of authority a court of equity has no inherent jurisdiction in such a case.⁵³ Such jurisdiction is some-

⁵² Post, p. 389.

⁵³ Strong v. McCagg, 55 Wis. 624, 13 N. W. 895; Hardon v. Newton, 14 Blatchf. 376, Fed. Cas. No. 6,054, 1 Cumming, Cas. Priv. Corp. 487; Hodges v. Screw Co., 3 R. I. 9; Verplanck v. Insurance Co., 1 Edw. Ch. (N. Y.) 84; Bayless v. Oure, 1 Freem. Ch. (Miss.) 161; State v. Merchants' Insurance & Trust Co., 8 Humph. (Tenn.) 235; Com. v. Union Fire & Marine Ins. Co., 5 Mass. 232; Folger v. Insurance Co., 99 Mass. 274; Neall v. Hill, 16 Cal. 145; Howe v. Deuel, 43 Barb. (N. Y.) 504; Waterbury v. Express Co., 50 Barb. 157; Belmont v. Railway Co., 52 Barb. 637; Denike v. Cement Co., 80 N. Y. 599.

"CAPITAL STOCK" AND "CAPITAL."

87. The "capital stock" of a corporation is the amount in money or property subscribed and paid in, or secured to be paid in, by the shareholders, and always remains the same unless changed by legislative authority

88. The "capital" of a corporation includes all the property of the corporation, and may therefore be greater or less in value than the capital stock.

The terms "capital" and "capital stock," as applied to corporations, are often used by the courts and in statutes as if they were synonymous, but, strictly speaking, they are not so. They do not mean the same thing. The capital stock of a corporation is the amount in money or property subscribed and paid in, or secured to be paid in, by the shareholders, and always remains the same unless changed by legislative authority.⁹ The capital of a corporation is a broader term, and includes all the funds, securities, credits, and property, of whatever kind, which the corporation possesses.¹⁰ Thus, if a banking corporation is organized with a capital stock of \$100,000, and after this is paid in it makes profits amounting to \$50,000, which it keeps instead of distributing it in the way of dividends, it has a capital of \$150,000, but its capital stock remains, as at the start, \$100,000. As was said by Chief Justice Green, capital stock, as employed in acts of incorporation, is never used

⁹ Christensen v. Eno, 106 N. Y. 97, 12 N. E. 648; State v. Morristown Fire Ass'n, 23 N. J. Law, 195; Williams v. Telegraph Co., 93 N. Y. 162, 188; Barry v. Exchange Co., 1 Sandf. Ch. (N. Y.) 280.

¹⁰ Christensen v. Eno, 106 N. Y. 97, 12 N. E. 648. "The word 'capital' is unambiguous. It signifies the actual estate, whether in money or property, which is owned by an individual or a corporation. In reference to a corporation, it is the aggregate of the sum subscribed and paid in, or secured to be paid in, by the shareholders, with the addition of all gains or profits realized in the use and investment of those sums, or, if losses have been incurred, then it is the residue after deducting such losses." People v. Commissioners of Taxes, etc., for the City and County of New York, 23 N. Y. 192, 219.

to indicate the value of the property of the company. It is very generally, if not universally, used to designate the amount of capital prescribed to be contributed at the outset by the stockholders for the purposes of the corporation. The value of the corporate assets may be greatly increased by surplus profits, or be diminished by losses, but the amount of the capital stock remains the same. The funds of the company may fluctuate; its capital stock remains invariable, unless changed by legislative authority.¹¹

NATURE OF SHARES OF STOCK.

89. A share of stock in a corporation is the right to partake, according to the amount put into the fund representing the capital stock, of the surplus profits of the corporation, and ultimately, on its dissolution, of so much of this fund as is not liable for the debts of the corporation.
90. A share of stock is in the nature of a chose in action, and it is personal property, though the corporation may own real estate. Thus
 - (a) A sale of shares is not within that clause of the statute of frauds requiring agreements for the sale of land or an interest therein to be in writing.
 - (b) On the death of the owner, shares are distributed as personal estate, and do not go to the heirs as real estate.
 - (c) In most states a sale of shares, like a sale of other choses in action, is within that clause of the statute of frauds relating to agreements for the sale of "goods, wares, and merchandises."
 - (d) Shares of stock, being intangible, and in the nature of choses in action, were not subject to execution at common law; but by statute they are now very generally made subject to execution and attachment.

¹¹ State v. Morristown Fire Ass'n, 23 N. J. Law, 195.

Shares of stock "are intangible, and rest in abstract legal contemplation."¹² When it is said that a person owns a certain number of shares of stock, it is meant that he has a right to share in the profits of the corporation, and in its property on dissolution, after payment of its debts, in the proportion that the number of his shares bears to the whole capital stock. A share of the capital stock is the right to partake, according to the amount put into the fund representing the capital stock, of the surplus profits of the corporation, and ultimately, on the dissolution of it, of so much of the fund thus created as remains unimpaired, and is not liable for the debts of the corporation.¹³

Shares of stock are not a chattel interest. The holders do not own the property of the corporation.¹⁴ They are in the nature of a chose in action.¹⁵ Thus shares of stock belonging to a married woman are not personal property in possession so as to vest in her husband at common law; but, like choses in action, they must be reduced to his possession.¹⁶

The fact that the corporation owns real estate, or even that all of its property is real estate, does not make the shares of its stock real property. They are in the nature of choses in action, and are personal property. It follows that an agreement for the sale of shares in a corporation owning real estate is not an agreement for the sale of land, or of an interest in land, so as to render writing necessary under the statute of frauds.¹⁷ So, on the death of a shareholder in a corporation, the capital stock of which is represented by real estate, his shares are to be distributed as personal estate, and do not go to the heirs as real property.¹⁸

¹² *Burrall v. Railroad Co.*, 75 N. Y. 211, 217.

¹³ *Burrall v. Railroad Co.*, 75 N. Y. 211, 216; *Ohio Life Insurance & Trust Co. v. Merchants' Insurance & Trust Co.*, 11 Humph. (Tenn.) 1; *Fisher v. Bank*, 5 Gray (Mass.) 373, 1 Cumming, Cas. Priv. Corp. 664.

¹⁴ Ante, p. 6 et seq.

¹⁵ *Fisher v. Bank*, 5 Gray (Mass.) 373, 1 Cumming, Cas. Priv. Corp. 664.

¹⁶ Tiff. Pers. & Dom. Rel. 89; Ang. & A. Corp. §§ 560, 561; *Slaymaker v. Bank*, 10 Pa. St. 373; *Arnold v. Ruggles*, 1 R. I. 165.

¹⁷ *Humble v. Mitchell*, 11 Adol. & E. 205, 1 Cumming, Cas. Priv. Corp. 602. And they will pass by a will not executed according to the provision of the statute of frauds relating to devises of land. *Bligh v. Brent*, 2 Younge & C. 268

¹⁸ *Russell v. Temple* (Mass.) 3 Dane, Abr. 108.

It is held in England that shares of stock are not "goods, wares, or merchandise," within the meaning of the seventeenth section of the statute of frauds, and that a contract for the sale thereof to the value of more than £10 need not be in writing, as the statute is there considered as referring to corporeal movable property only, and not as including choses in action which are incapable of part delivery.¹⁹ In this country some of the courts have followed the English rule;²⁰ but in most states the construction placed upon the statute is different, and it is held to include incorporeal as well as corporeal property, and therefore to include shares of stock.²¹ In some states the statute is broader in its terms than the original statute. In New York and several other states it expressly includes choses in action, and in Florida it uses the term "personal property," and these statutes of course apply to stock in corporations.²²

Execution and Attachment.

A share of stock, being in the nature of a chose in action, could not be reached by execution at common law, and it is not subject to attachment, unless expressly made so by statute.²³ In most states, however, if not in all, statutes have been enacted, making shares of stock and other choses in action subject to execution, and the statutes providing for attachment generally make shares of stock subject to that remedy. It is not necessary that the statute shall expressly mention shares of stock. If it uses terms clearly showing

¹⁹ *Humble v. Mitchell*, 11 Adol. & E. 205, 1 Cumming, Cas. Priv. Corp. 602; *Knight v. Barber*, 16 Mees. & W. 66.

²⁰ *Webb v. Railroad Co.*, 77 Md. 92, 26 Atl. 113; *Whittemore v. Gibbs*, 24 N. H. 484; *Vawter v. Griffin*, 40 Ind. 593.

²¹ *Tiff. Sales*, 43, 44; *Clark*, Cont. 138; *Tisdale v. Harris*, 20 Pick. (Mass.) 9, 1 Cumming, Cas. Priv. Corp. 604; *Boardman v. Cutter*, 128 Mass. 388; *North v. Forest*, 15 Conn. 400; *Pray v. Mitchell*, 60 Me. 430; *Hinchman v. Lincoln*, 124 U. S. 38, 8 Sup. Ct. 369; *Greenwood v. Law*, 55 N. J. Law, 168, 26 Atl. 134; *Hudson v. Weir*, 29 Ala. 294; *Green v. Brookins*, 23 Mich. 48, 54.

²² *Artcher v. Zeh*, 5 Hill (N. Y.) 200; *Peabody v. Speyers*, 56 N. Y. 230; *Mayer v. Child*, 47 Cal. 142; *Spear v. Bach*, 82 Wis. 192, 52 N. W. 97; *Southern Life Insurance & Trust Co. v. Cole*, 4 Fla. 359.

²³ 1 *Cook, Stock, Stockh. & Corp. Law*, §§ 480-491; *Denton v. Livingston*, 9 Johns. (N. Y.) 96; *Blair v. Compton*, 33 Mich. 414; *Van Norman v. Jackson Circuit Judge*, 45 Mich. 204, 7 N. W. 796; *Barnes v. Hall*, 55 Vt. 420; *State Ins. Co. v. Sax*, 2 Tenn. Ch. 507, 509; *Goss & P. Manuf'g Co. v. People*, 4 Ill. App. 510; *Haley v. Reid*, 16 Ga. 437; *Foster v. Potter*, 37 Mo. 525.

an intention to include such property, it will be given effect accordingly. Thus shares of stock would clearly be included under the term "choses in action." They have been held to be included under the terms "estate,"²⁴ "rights and credits."²⁵ But there are some cases in which the statutes are more strictly construed, and in which shares of stock have been held not to be included under the phrase "real and personal property," or "estate, both real and personal."²⁶

To render a levy of execution or attachment on shares of stock and a sale thereunder valid, the provisions of the statute as to the mode of making the levy and sale, and the formalities to be observed, must be strictly observed.²⁷

The situs of shares of stock for most purposes is in the state by which the corporation was created, and they can be levied upon in that state only.²⁸

CERTIFICATES OF STOCK.

91. A certificate of stock is simply a written acknowledgment by the corporation of the interest of the holder in its property and franchises.

²⁴ *Chesapeake & O. R. Co. v. Paine*, 29 Grat. (Va.) 502, 505. And see *Union Nat. Bank v. Byram*, 131 Ill. 92, 22 N. E. 842.

²⁵ *Curtis v. Steever*, 36 N. J. Law, 304.

²⁶ *Haley v. Reid*, 16 Ga. 437; *Foster v. Potter*, 37 Mo. 525. But see *Union Nat. Bank v. Byram*, 131 Ill. 92, 22 N. E. 842.

²⁷ 1 Cook, Stock, Stockh. & Corp. Law, § 481; *Titcomb v. Insurance Co.*, 8 Mass. 326; *Howe v. Starkweather*, 17 Mass. 240; *Blair v. Compton*, 33 Mich. 414; *Van Norman v. Jackson Circuit Judge*, 45 Mich. 204, 7 N. W. 796; *Morton v. Graffin*, 68 Md. 545, 13 Atl. 341; *Voorhis v. Terhune*, 50 N. J. Law, 147, 13 Atl. 391; *Armour Bros. Banking Co. v. St. Louis Nat. Bank*, 113 Mo. 12, 20 S. W. 691; *Moore v. Opera-House Co.*, 81 Iowa, 45, 46 N. W. 750; *Commercial Nat. Bank v. Farmers' & Traders' Nat. Bank*, 82 Iowa, 192, 47 N. W. 1080; *Keating v. Stock Co.*, 88 Tex. 467, 18 S. W. 797; *McNaughton v. McLean*, 73 Mich. 250, 41 N. W. 267; *Goss & P. Manuf'g Co. v. People*, 4 Ill. App. 510; *People v. Goss & Phillips Manuf'g Co.*, 99 Ill. 355.

²⁸ 1 Cook, Stock, Stockh. & Corp. Law, § 485; *Plimpton v. Bigelow*, 93 N. Y. 592; *Armour Bros. Banking Co. v. St. Louis Nat. Bank*, 113 Mo. 12, 20 S. W. 691. Compare *Young v. Iron Co.*, 85 Tenn. 189, 2 S. W. 202.

Shares in the capital stock of a corporation are usually represented by certificates issued by the corporation to the stockholders, stating that the holder is the owner of a certain number of shares, and generally prescribing the mode in which they may be transferred, as on the books of the company in person or by attorney, and on surrender of the certificate. A stock certificate is merely evidence of the stockholder's rights. "The issuing of the original certificates is in no sense a transfer of stock. The interest of the parties to whom they are issued is the same before as after such issue. The certificate is simply a written acknowledgment by the company of the interest of the subscribers in its property and franchises."²⁹ A certificate of stock is not a security, much less a negotiable instrument.³⁰ It is not necessary to constitute a subscriber a stockholder.³¹

SUBSCRIPTIONS TO STOCK—SUBSCRIPTIONS AFTER INCORPORATION.

92. A subscription to the stock of an existing corporation, when accepted, is a contract between the subscriber and the corporation, and is subject to the rules governing other kinds of contracts.

When a corporation is already organized, a subscription to its capital stock is like any other contract with the corporation. It is a contract between the corporation and the subscriber, and is subject to the principles governing the formation of other contracts. There must be an offer by one party and acceptance by the other, resulting in mutual agreement. If the corporation opens subscription books or solicits subscriptions, and a person subscribes for shares, he makes an offer to the corporation; and when the subscription or offer is accepted by the corporation, it becomes binding. Or the solicitation of subscriptions may be a general offer by the corporation, and a subscription in accordance with the offer would be an acceptance, and result in a contract without further assent on

²⁹ Burr v. Wilcox, 22 N. Y. 551, 557. ³⁰ Post, p. 427. ³¹ Post, p. 316.

the part of the corporation.⁸² In these cases there is a contract between the subscriber and the corporation, which ipso facto makes the subscriber a shareholder, and binds him to pay the amount of the subscription.⁸³

There must also be a consideration for the promise of the subscriber and for the undertaking of the corporation to recognize him as a stockholder. The consideration for the latter is the subscriber's promise to pay for his stock, and the consideration for the former is the acquisition by the subscriber of an interest in the franchises and property of the corporation and the right to share in the profits.⁸⁴ It follows that the obligation must be mutual. "A stock subscription is a transaction between the subscriber and the company, and the obligation of one can only be sustained by the corresponding obligation of the other. If both are not bound, neither is bound, and the transaction is a nullity."⁸⁵

Distinguished from a Sale of Shares.

A subscription to the capital stock of a corporation after its organization must be distinguished from a sale of shares by it. A purchase of shares, if fully executed, will make the purchaser a stockholder, but it does not make him a subscriber; and the rules governing subscriptions and sales of shares are different. Thus, as we shall see, in the case of a subscription, failure of the corporation to issue or tender a certificate of stock, which is merely evidence of

⁸² Greer v. Railway Co., 96 Pa. St. 391. In this case plaintiff opened books for subscriptions, placing one of them in the defendant's hands for solicitation of subscriptions. Defendant entered his own name on the book as a subscriber, and kept the book for six months without attempting to withdraw his name. He then cut his name out, and returned the book to plaintiff. He claimed that he had a right to withdraw at any time before he returned the book, but it was held that the contract of subscription was binding upon him, because the company, in soliciting subscriptions, "made a continuing offer, which became an agreement with each acceptant for the number of shares for which he subscribed."

⁸³ Hartford & N. H. R. Co. v. Kennedy, 12 Conn. 499, 506; Spear v. Crawford, 14 Wend. (N. Y.) 20; Walter A. Wood Harvester Co. v. Robbins, 56 Minn. 48, 57 N. W. 317, W. D. Smith, Cas. Corp. 44; McClure v. Railway Co., 90 Pa. St. 269.

⁸⁴ Post, p. 267.

⁸⁵ Per Campbell, J., in Carlisle v. Railroad Co., 27 Mich. 315, 318.

the ownership of shares, does not prevent the subscriber from becoming a shareholder, with all the rights and subject to all the liabilities of shareholders, unless there is a stipulation to that effect in the subscription.⁸⁶ On a sale of stock, however, the rule is different. Such a sale stands on the same footing as a sale of any other property, and tender of the certificate is a condition precedent to the right to maintain an action for the price.⁸⁷

SAME—SUBSCRIPTIONS PRIOR TO INCORPORATION.

- 93.** A preliminary agreement by a number of persons to form a corporation and take stock therein is not a contract by the subscribers with each other, and cannot be enforced by one or more against any other, but is enforceable only by the corporation when formed.
- 94.** Such an agreement, if not made as a step authorized by statute in the process of forming the corporation, is a mere continuing offer to the corporation by each subscriber, and may be revoked, or will lapse on the subscriber's death or insanity at any time before the corporation is organized. But the organization of the corporation before revocation or lapse operates as an acceptance of the offer, and the subscriptions then become binding and irrevocable, and may be enforced by the corporation.
- 95.** Such an agreement, if made as a step authorized by statute in the process of forming the corporation, is valid by virtue of the statute, though there is no consideration or mutuality prior to the organization of the corporation, and is binding on each subscriber from the time of signing, and is irrevocable

⁸⁶ Post, p. 316; *Marson v. Deither*, 49 Minn. 423, 52 N. W. 38.

⁸⁷ Post, p. 317; *Marson v. Deither*, supra; *Clark v. Improvement Co.*, 57 Ind. 185. And see *Thrasher v. Railroad Co.*, 25 Ill. 393; *St. Paul, S. & T. F. R. Co. v. Robbins*, 23 Minn. 439; *Weiss v. Iron Co.*, 58 Pa. St. 295.

thereafter; but it can be enforced only by the corporation.

96. An agreement to pay money to trustees to be by them paid to a corporation thereafter to be created, the trustees to return to the subscribers stock in the corporation, is a valid contract between the subscribers and the trustees.⁸⁸

97. Some of the courts make a distinction between a present subscription to the stock of a corporation to be formed and an agreement to subscribe at a future time. According to these cases, the former renders the party a stockholder, and liable on his subscription, when the corporation is organized; but the latter merely renders him liable to an action for damages on failure to take stock, the measure of damages being the difference between the market and par value of the stock.

The usual method of subscribing to the stock of a corporation which it is proposed to organize is for the parties to sign an agreement to form the corporation, and take stock in it when formed. Sometimes, but not always, they in terms promise to pay the amount of their subscriptions to the corporation. The better opinion is that such an agreement, at least in so far as the promises to subscribe are concerned, is not a contract by the subscribers with each other, and cannot be enforced by one or more of them against any other.

Common-law Subscriptions.

If the agreement is not made as a step authorized by statute in the process of forming the corporation, but depends upon the common law, it is a mere offer by each subscriber to the corporation not yet in existence to take stock, and thereby become a shareholder; and when the corporation is organized and accepts the offer, there is a binding contract of subscription between the corporation and the subscriber, by virtue of which, ipso facto, the subscriber be-

⁸⁸ The above propositions are taken in substance from Prox. Collin's syllabus for his class on Corporations in the Cornell University Law School.

comes a shareholder, with all the rights and privileges, and subject to all the liabilities, of a shareholder, and the subscription may be enforced by the corporation.³⁹ Before the corporation is formed, the subscriptions, as we shall see, are not binding, for there is no consideration or mutuality; and, besides this, the other party to the contract is not yet in existence. But the formation of the corporation and acceptance of the subscriptions supplies the element of consideration and the other party, and renders them binding.

In *Strasburg R. Co. v. Echternacht*⁴⁰ it was held by the supreme court of Pennsylvania that such a subscription could not result in a contract between the subscriber and the corporation when formed, so as to entitle the corporation to maintain an action on it, since it was thought that the nonexistence of the corporation at the time of signing the subscription rendered the formation of a contract with it in this way impossible. This decision, if it has not been in effect overruled by later decisions of the Pennsylvania court,⁴¹ is in conflict with the decisions in almost all of the other states. It is not at all necessary, as was assumed in the case referred to, that a contract shall result, if at all, at the time the offer or proposal is made. A continuing offer may be made, and a contract will result when it is subsequently accepted according to its terms. Nor is it necessary that an offer, to result in a contract, shall be

³⁹ *Athol Music Hall Co. v. Carey*, 116 Mass. 471; *Penobscot R. Co. v. Dummer*, 40 Me. 172; *Danbury & N. R. Co. v. Wilson*, 22 Conn. 435; *Richelieu Hotel Co. v. International Military Enc. Co.*, 140 Ill. 248, 29 N. E. 1044, W. D. Smith, Cas. Corp. 48, Shep. Cas. Corp. 16; *Tonica & P. R. Co. v. McNeely*, 21 Ill. 71; *Marysville Electric Light & Power Co. v. Johnson*, 93 Cal. 538, 29 Pac. 126; *Buffalo & N. Y. C. R. Co. v. Dudley*, 14 N. Y. 336; *Buffalo & J. R. Co. v. Gifford*, 87 N. Y. 294; *Instone v. Bridge Co.*, 2 Bibb (Ky.) 576; *Bullock v. Turnpike Co.*, 85 Ky. 184, 3 S. W. 129; *Gleaves v. Turnpike Co.*, 1 Sneed (Tenn.) 491; *Chaffin v. Cummings*, 37 Me. 76, 83; *Schaeffer v. Insurance Co.*, 46 Mo. 248; *Red Wing Hotel Co. v. Friedrich*, 26 Minn. 112, 1 N. W. 827; *Taggart v. Railroad Co.*, 24 Md. 503; *Hughes v. Manufacturing Co.*, 34 Md. 316, 326; *Low v. Railroad Co.*, 45 N. H. 370; *Ashuelot Boot & Shoe Co. v. Hoit*, 56 N. H. 548, 556.

⁴⁰ 21 Pa. St. 220, 60 Am. Dec. 49.

⁴¹ See *Edinboro Academy v. Robinson*, 37 Pa. St. 210; *Hedge's & Horn's Appeal*, 63 Pa. St. 273; *McClure v. Railway Co.*, 90 Pa. St. 269; *Shober's Adm'rs v. Lancaster Co. Park Ass'n*, 68 Pa. St. 429; *Steamship Co. v. Murphy*, 6 Phila. 224.

made to an ascertained person.⁴² Therefore, while it is true that a subscription to the capital stock of a corporation not yet formed is not, and cannot be, a contract with the corporation at the moment the subscription paper is signed, the corporation not being then in existence, this does not prevent its resulting in a contract at a subsequent time. It is a continuing offer or proposal on the part of the subscriber to take shares in the corporation when formed, and, by the weight of authority,⁴³ to pay the amount of the subscription; and when the corporation is organized as contemplated, before the offer is withdrawn, and accepts the subscription, it then becomes a binding contract between the subscriber and the corporation.

In *Athol Music Hall Co. v. Carey*⁴⁴ the defendant and others signed a written agreement by which, in terms, they severally promised and agreed to and with each other that they would associate themselves into a corporation, and pay to the treasurer of the corporation the amount of the several shares set against their respective names; and it was held that the corporation, when it was organized and accepted the promises, could maintain an action against the subscribers on the agreement. "In agreements of this nature," it was said, "entered into before the organization is formed, or the agent constituted to receive the amounts subscribed, the difficulty is to ascertain the promisee, in whose name alone suit can be brought. The promise of each subscriber, 'to and with each other,' is not a contract capable of being enforced between each subscriber and each other who may have signed previously, or who should sign afterwards, nor between each subscriber and all the others collectively as individuals. The undertaking is inchoate and incomplete as a contract until the contemplated organization is effected, or the mutual agent constituted to represent the association of individual rights in accepting and acting upon the propositions offered by the several subscriptions. When thus accepted, the promise may be construed to have legal effect according to its purpose and intent,

⁴² See *Anson*, Cont. 31; *Clark*, Cont. 55.

⁴³ *Post*, p. 318.

⁴⁴ 116 Mass. 471.

and the practical necessity of the case, to wit, as a contract with the common representative of the several associates.”⁴⁵

Some of the courts regard an agreement by a number of persons to subscribe for stock in a corporation to be formed as a contract between the parties for the benefit of the corporation when formed, and allow the corporation to maintain an action thereon as upon a contract made for its benefit.⁴⁶ This view, however, could not be sustained in those jurisdictions where, as at common law, a person for whose benefit a contract is made, but who is not a party to it, cannot maintain an action thereon.

Consideration for Subscription.

At common law a consideration is just as essential to a contract of subscription, and to the express or implied promise of the subscriber to pay the same, as in the case of any other kind of contract. It might be rendered unnecessary in the case of an existing corporation by subscribing under seal in those jurisdictions where a seal dispenses with the necessity for a consideration.⁴⁷ And, as will be presently seen, the legislature, in providing for subscriptions preliminary to the organization of a corporation, may expressly or impliedly make them binding without a consideration.⁴⁸ Except in these cases, a subscription is not binding unless there is a sufficient consideration. In the case of subscriptions to stock a consideration arises from the benefit received by the subscriber in acquiring an interest in the corporate franchises and property, and a right to share in the profits, or, as it has been otherwise expressed, there is a consideration in the title which the subscriber acquires to shares.⁴⁹

⁴⁵ And see the other cases cited in note 39, *supra*.

⁴⁶ See *Marysville Electric Light & Power Co. v. Johnson*, 93 Cal. 538, 29 Pac. 126; *International Fair & Exp. Ass'n v. Walker*, 83 Mich. 386, 47 N. W. 338.

⁴⁷ *Hudson Real-Estate Co. v. Tower*, 156 Mass. 82, 30 N. E. 465.

⁴⁸ *Post*, p. 271.

⁴⁹ *Walter A. Wood Harvester Co. v. Robbins*, 56 Minn. 48, 57 N. W. 317, *W. D. Smith, Cas. Corp.* 44; *Buffalo & N. Y. City R. Co. v. Dudley*, 14 N. Y. 336; *Worcester Turnpike Corp. v. Willard*, 5 Mass. 80; *Athol Music Hall Co. v. Carey*, 116 Mass. 471; *Griswold v. Trustees*, 26 Ill. 41; *Gleaves v. Turnpike Co.*, 1 Sneed (Tenn.) 491; *East Tennessee & V. R. Co. v. Gammon*, 5 Sneed. (Tenn.) 567; *Selma & T. R. Co. v. Tipton*, 5 Ala. 787; *Danbury & N. R. Co. v. Wilson*, 22 Conn. 435; *Instone v. Frankfort Bridge Co.*, 2 Bibb. (Ky.) 576.

It follows that a subscription, to be binding on the subscriber, must be binding on the corporation, so that it is bound to recognize the subscriber as a shareholder. In *Fanning v. Insurance Co.*⁵⁰ the defendant, prior to the organization of the plaintiff corporation, orally promised to take shares of stock, and gave her note to pay therefor, and the plaintiff brought an action on the note after its organization. The court held that the verbal subscription was not sufficient to make the defendant a shareholder, and that, therefore, there was no consideration for her promise.

It has been said that there is a consideration for a subscription in the corresponding promises of the other subscribers,⁵¹ but this is not true. It is not a case of mutual promises, where the promise of one party forms the consideration for the promise of the other. The promises are all to the corporation. Each is, as we have seen, an offer to the corporation until it is organized and accepts it. Then it becomes a promise to it, not to the other subscribers. One subscriber is not liable to an action by the others on his subscription.

Revocation or Lapse of Subscription.

As we have just seen, in the case of subscriptions, or rather offers to subscribe, to the stock of a proposed corporation, until the corporation is organized and accepts the subscription, it is not binding at common law, for the reason, among others, that until then there is no consideration for it. There is no mutuality. Until the corporation is bound to recognize the subscriber as a shareholder, he receives no consideration for his subscription. It follows, necessarily, from this that the offer to subscribe may be revoked or withdrawn by the subscriber at any time before the corporation is organized and accepts it, or before organization if that alone constitutes acceptance so as to make the subscriber a shareholder.⁵²

⁵⁰ 37 Ohio St. 339.

⁵¹ *Athol Music Hall Co. v. Carey*, 116 Mass. 471; *Tonica & P. R. Co. v. McNeely*, 21 Ill. 71; *Carlisle v. Railroad Co.*, 27 Mich. 315.

⁵² *Hudson Real-Estate Co. v. Tower*, 156 Mass. 82, 30 N. E. 465; *Id.*, 161 Mass. 10, 36 N. E. 680, *W. D. Smith, Cas. Corp.* 45, *Shep. Cas. Corp.* 23; *Wallace v. Townsend*, 43 Ohio St. 537, 3 N. E. 601; *Muncy Traction Engine Co. v. De La Green* (Pa. Sup.) 13 Atl. 747; *Auburn Bolt & Nut Works v. Shultz*, 143 Pa. St. 256, 22 Atl. 904; *Lewis v. Mill Co.* (Tex. Civ. App.) 23 S. W. 338;

It also follows that the offer to subscribe will be revoked or lapse if the subscriber dies or becomes insane before the corporation is organized and accepts it, for the continuance of an offer is in the nature of its constant repetition, which necessarily requires some one capable of making a repetition, and this can no more be done by a dead or insane man than a contract can, in the first instance, be made by a dead or insane man.⁵³

Not only is such an offer revocable because of the want of consideration, but it is revocable for the further reason that until the corporation is organized there cannot, in the nature of things, be any contract, since one of the parties—the corporation—is not yet in existence. The right to revoke exists, therefore, where the subscription is under seal.⁵⁴

In order that withdrawal of a subscription may be effectual, it is necessary, as in the case of other contracts, that notice thereof shall be communicated. An uncommunicated revocation can have no effect whatever. It is not necessary that the notice of revocation be given to all the other subscribers, nor at a meeting of subscribers. It is sufficient if it be given to the person or persons to whom the subscription was given, or to the person or persons who have been chosen to represent the subscribers in forming the corporation.⁵⁵ It

Patty v. Mill Co., 4 Tex. Civ. App. 224, 23 S. W. 336; *Plank's Tavern Co. v. Burkhard*, 87 Mich. 182, 49 N. W. 562.

⁵³ *Pratt v. Trustees*, 93 Ill. 475; *Beach v. First Methodist Episcopal Church*, 96 Ill. 177; *Phipps v. Jones*, 20 Pa. St. 260; *Wallace v. Townsend*, 43 Ohio St. 537, 8 N. E. 601.

⁵⁴ "Until the organization of the corporation, the subscription is a mere proposition or offer, which may be withdrawn, like any other unaccepted offer. Unless the signer is bound upon a contract, he is not bound at all. It is open to him to withdraw. It is not on the ground that there was no sufficient consideration. The seal would do away with any doubt on that score. But it is on the ground that for the time being, and until the corporation is organized, the writing does not take effect as a contract, because the contemplated party to the contract, on the other side, is not yet in existence, and for this reason, there being no contract, the whole undertaking is inchoate and incomplete, and, since there is no contract, the party may withdraw." *Hudson Real-Estate Co. v. Tower*, 156 Mass. 82, 30 N. E. 465; *Id.*, 161 Mass. 10, 36 N. E. 680, W. D. Smith, Cas. Corp. 45; *Shep. Cas. Corp.* 23.

⁵⁵ *Hudson Real-Estate Co. v. Tower*, 161 Mass. 10, 36 N. E. 680, W. D. Smith, Cas. Corp. 45, *Shep. Cas. Corp.* 23. In *Hudson Real-Estate Co. v. Tow-*

was held in an early English case that all the other subscribers must not only have notice, but must consent, before one of the subscribers can withdraw;⁵⁶ but now, in England as well as in this country, such consent is unnecessary. If all the other subscribers should object, it would nevertheless be the right of a subscriber to withdraw before the corporation is formed.⁵⁷

Since, upon organization of the corporation and acceptance of subscriptions, they are changed into binding contracts, a subscriber cannot afterwards withdraw without the consent of the corporation and of all the other subscribers; nor will his subscription be affected by his death or insanity after that time.⁵⁸

The supreme court of Minnesota has held in a late case as follows: "A subscription by a number of persons to the stock of a corporation to be thereafter formed by them has in law a double character: First. It is a contract between the subscribers themselves to become stockholders without further act on their part immediately upon the formation of the corporation. As such a contract it is binding and irrevocable from the date of the subscription (at least in the absence of fraud or mistake), unless canceled by consent of all the subscribers before acceptance by the corporation. Second. It is also in the nature of a continuing offer to the proposed corporation, which, upon acceptance by it after its formation, becomes as to each subscriber a contract between him and the corporation." And it was further held that the promoter of a proposed corporation, who solicits and procures subscriptions, is the agent of the body of subscribers to hold the subscriptions until the corporation is formed, and then turn them over

er, *supra*, the defendants subscribed under seal for stock in a corporation. Afterwards articles of incorporation were executed, and officers elected; but, before the incorporation was complete, the defendants orally informed the president that, if a certain change in the policy was made, they would no longer be associates, and would not pay their subscriptions. The change of policy was made, and it was held that was a sufficient withdrawal by the defendants, and notice thereof.

⁵⁶ *Kidwelly Canal Co. v. Raby*, 2 Price, 93.

⁵⁷ *Hudson Real-Estate Co. v. Tower*, 161 Mass. 10, 36 N. E. 680, W. D. Smith, Cas. Corp. 45, Shep. Cas. Corp. 23.

⁵⁸ *Richellieu Hotel Co. v. International Military Enc. Co.*, 140 Ill. 248, 29 N. E. 1044, W. D. Smith Cas. Corp. 48, Shep. Cas. Corp. 16; *Athol Music Hall Co. v. Carey*, 116 Mass. 471; *post*, p. 329.

to it without any further act of delivery on the part of the subscribers; and hence, that a delivery of a subscription to such promoter is a complete delivery, so that it becomes eo instanti a binding contract as between the subscribers.⁵⁹ This decision is sound in so far as it holds that the subscriptions are continuing offers to the proposed corporation, and become binding when it is organized and accepts them; but it is opposed to the weight of authority in so far as it holds that an agreement by a number of persons to subscribe to the stock of a proposed corporation is a contract between the subscribers, and binding upon them, so as to be irrevocable before the corporation is organized. The authorities cited by the court do not sustain this view.

Subscriptions under Statutes.

Thus far we have been speaking of those agreements to form a corporation and subscribe for stock that depend upon common-law principles only, and that are not made as a step authorized by statute in the process of forming the corporation. Such an agreement made as a step authorized by statute in the process of forming the corporation stands upon a somewhat different ground. Like the agreements of which we have been speaking, it can only be enforced by the corporation after its organization; but it is binding on each subscriber, by virtue of the statute, from the time of signing, and he cannot revoke his subscription before the corporation is completely organized. In *Buffalo & New York Railroad Co. v. Dudley*⁶⁰ a railroad company had been organized under a statute which appointed commissioners to open books and receive subscriptions to its capital stock. The defendant, among others, subscribed on the books, and otherwise complied with the statute. The corporation was completely organized, and accepted the subscriptions before the defendant attempted to withdraw his, and therefore his subscription could be sustained as a continuing offer accepted by the corporation, and thereby changed into a binding promise supported by a sufficient consideration; but the court went further than this, and said that no consideration or mutuality was necessary, and that the subscription could not have been revoked even before the corporation was organized. "The rules

⁵⁹ *Minneapolis Threshing Mach. Co. v. Davis*, 40 Minn. 110, 41 N. W. 1026.

⁶⁰ 14 N. Y. 336.

of the common law," it was said, "in regard to consideration and mutuality, do not apply to the case. Those rules may, I think, be regarded as superseded by the statute, which not only expressly authorizes subscriptions to be made in anticipation of the existence of the corporation, but impliedly, at least, recognizes their validity. Section 4 of the act by which the plaintiffs are incorporated provides, among other things, as follows: 'And the said commissioners shall, at the time of any subscription, require the payment to them, by the person or persons subscribing, of five dollars towards and upon every hundred dollars so subscribed, and unless the same shall be paid, the subscription shall be invalid.' This plainly implies that, if the required payment is made, the subscription shall be valid. But even without this clause it would, I think, be held that a statute which authorizes subscriptions in view of a subsequent incorporation, and regulates the manner in which they shall be made, must necessarily have the effect to give validity to such subscriptions, if made in accordance with the requirements of the act." The same principle applies where the statute provides for subscriptions by signing formal articles of association, which are to be filed as required by the statute, or formal subscription papers. One who subscribes for stock by signing such articles or papers in compliance with the statute cannot revoke his subscription before the incorporation is perfected.⁶¹

Agreements to Pay Subscription to Trustees for Corporation when Formed.

"An agreement to pay money to trustees, to be by them paid to a corporation thereafter to be created, the trustees to return to the subscribers stock in the corporation accordingly, is a valid contract between the subscribers and the trustees."⁶² In *West v. Crawford*⁶³ the defendant and others entered into an agreement to form a corporation, and to take a certain number of shares of the stock, and expressly promised to pay a certain percentage of the par value thereof to one West within five days after filing of the articles of in-

⁶¹ *Lake Ontario, A. & N. Y. R. Co. v. Mason*, 16 N. Y. 451; *Johnson v. Wabash & Mt. Vernon Plank-Road Co.*, 16 Ind. 389; *Coppage v. Hutton*, 124 Ind. 401, 24 N. E. 112; *Greenbrier Industrial Exposition v. Rodes*, 37 W. Va. 738, 17 S. E. 305.

⁶² Prof. Collin's Syllabus, Cornell Univ. Law School.

⁶³ 80 Cal. 19, 21 Pac. 1123.

corporation, and they constituted the said West their agent to collect the amount which might become due from them. It was held that West could maintain an action against them on their express promise as trustee of an express trust; and in a later case,⁶⁴ the corporation having been formed, and the money having been collected by West, it was held that the corporation could maintain an action against him for the same as money received by him to its use. It was held that the fact that the defendants did not sign the articles of incorporation, or otherwise comply with the statute under which the corporation was formed, and did not, therefore, become members of the corporation, was immaterial, as their liability to West was based on their express promise to pay the money to him for the use of the corporation. The agreement was sustained on the ground that the promises of the parties were mutual, and each was a consideration for the others.⁶⁵

Distinction between Present Subscription and Agreement to Subscribe.

Some of the courts make a distinction between a present subscription to the stock of a projected corporation and a mere agreement to subscribe, and the distinction has been recognized and approved by Mr. Morawetz and other writers on the law of corporations. The former, it is held, makes the parties stockholders, and renders them liable to the corporation on their promises, when it is organized. But the latter, it is held, is not a subscription or offer to the future corporation, but merely an agreement between the parties that they will subscribe at some future time; and until they do actually subscribe upon the books, or in some other formal way, no binding contract of subscription with the corporation can result.⁶⁶ In *Thrasher v. Pike County R. Co.*⁶⁷ the defendant and others signed a paper as follows: "We, the undersigned, agree to subscribe to the stock of the Pike County Railroad the sums set against our names, when the books may be opened for subscriptions." The corporation brought an action on this agreement, counting upon the agreement as a promise to subscribe, and alleging a failure to subscribe as a breach, and plaintiff claimed to recover the par value of the shares for which the defendant agreed to subscribe, or

⁶⁴ *San Joaquin Land & Water Co. v. West*, 94 Cal. 390, 29 Pac. 785.

⁶⁵ And see *Hecla Consolidated Gold Min. Co. v. O'Neill*, 65 Hun, 619, 19 N. Y. Supp. 592.

⁶⁶ 1 Mor. Corp. §§ 46, 49.

⁶⁷ 25 Ill. 898.

the amount of calls made upon the stock. It was held that it could not recover on such a cause of action, as the promise set up in the declaration was merely an agreement to subscribe when subscription books should be opened, and did not make the defendant a stockholder, so as to be liable to calls. The promise was regarded as like an agreement to purchase property, rendering him liable only for the actual loss sustained by plaintiff by reason of his failure to take the stock.⁶⁸

It is very doubtful whether this distinction is sound. Prof. Collin says that it is unsound, and disappears as mere dicta upon a thorough sifting of the cases.⁶⁹ Every agreement to subscribe to the stock of a corporation to be organized, unless there is a failure to comply with statutory requirements, should be held a continuing offer to the corporation, resulting in a binding contract of subscription when the corporation is organized as contemplated.⁷⁰

⁶⁸ See, also, *Stowe v. Flagg*, 72 Ill. 397, 402; *Quick v. Lemon*, 105 Ill. 578, 585. In *Mt. Sterling Coal-Road Co. v. Little*, 14 Bush. (Ky.) 429, the defendant signed the following writing: "The undersigned propose to subscribe for the number of shares, of \$50 each, to the capital stock of the Mt. Sterling Coal-Road Company, when the charter shall have been obtained and the company organized," etc. It was held, following *Thrasher v. Pike County R. Co.*, *supra*, that this was not a subscription, but an agreement to subscribe, for breach of which the plaintiff could only recover as damages the difference between the market and par value of the stock. In *Rhey v. Plank-Road Co.*, 27 Pa. St. 261, the defendant, to induce the plaintiff to locate its road along a certain route, signed an agreement that, if it should do so, one O'Neil "will subscribe \$500 additional stock, for which I hold myself personally responsible." The road having been located, the plaintiff sued defendant for breach of the contract. It was held that it could not recover the par value of the stock, but only the damages resulting from failure to take the stock, the measure of which was the difference between the par value and the actual value of the stock. In *Lake Ontario Shore R. Co. v. Curtiss*, 80 N. Y. 219, the defendant and others signed the following instrument: "We, the undersigned, citizens of Unionville and vicinity, pledge ourselves to subscribe for and take stock in and for the construction of the Lake Ontario Shore Railroad, to the amount set opposite our names, respectively, on condition said road be located and built through, or north of, the village of Unionville." It was held that this was not a subscription, but a mere agreement between the signers, to which the corporation was not a party, and upon which it could not maintain an action.

⁶⁹ Syllabus for Class in Corporations in Cornell University Law School.

⁷⁰ See *Bullock v. Railroad Co.*, 85 Ky. 184, 3 S. W. 129, qualifying *Mt. Sterling Coal-Road Co. v. Little*, *supra*.

SAME—WHO MAY BECOME SUBSCRIBERS.

98. Any person who is capable of contracting may subscribe for stock in a corporation, in the absence of express restrictions in the charter or act under which the corporation is organized.

The charter or act under which a corporation is organized may require the subscribers to its stock to be residents of the state or of the United States, or impose other restrictions. But, in the absence of such restrictions, any person who is capable of entering into a binding contract may become a subscriber. It makes no difference that he is a nonresident of the state, or an alien.⁷¹

An infant may subscribe for shares in a corporation, but he may repudiate the contract either before or after attaining his majority, provided, in the latter case, he has not ratified it before electing to disaffirm.⁷² If he elects to disaffirm, he must do so within a reasonable time after his majority, and before accepting benefits under the contract after majority, or he will be held to have ratified the contract, and will be liable for calls.⁷³ As we shall see, where the statute under which a corporation is formed requires that a certain amount of stock shall be subscribed before organization, there must be unconditional and binding subscriptions to that amount, and subscriptions by infants cannot be counted.⁷⁴

Persons non compotes mentis, whether their incapacity is the result of insanity, idiocy, senile dementia, or drunkenness, may avoid their stock subscriptions to the same extent, and subject to the same qualifications, as in the case of any other contract.

Where the common law in regard to the contractual capacity of married women still obtains, a subscription by a married woman is

⁷¹ Com. v. Hemingway, 131 Pa. St. 614, 18 Atl. 990.

⁷² Tiff. Pers. & Dom. Rel. 376; London & N. W. Ry. Co. v. M'Michael, 20 Law J. Exch. 97; Ebbett's Case, 5 Ch. App. 302; Lumsden's Case, 4 Ch. App. 31.

⁷³ Tiff. Pers. & Dom. Rel. 376; Clark, Cont. 241; Lumsden's Case, supra; Ebbett's Case, supra; Cork & B. Ry. Co. v. Cazenove, 10 Q. B. 935; Mitchell's Case, L. R. 9 Eq. 363; Dublin & W. Ry. Co. v. Black, 8 Exch. 181.

⁷⁴ Post, p. 308.

absolutely void.⁷⁵ In some states, by statute, a married woman may contract to the same extent as a feme sole, and in such a case she may bind herself by a stock subscription. In other states her incapacity has only been partially removed. Whether she can subscribe for stock in these states must depend upon the particular statute, and the extent to which it has removed her common law disabilities.⁷⁶ Independently of any statute, a married woman may take shares by purchase, gift, or bequest, and hold the same, just as she may take and hold any other chose in action.⁷⁷ And in such a case she will incur statutory liability as a stockholder.⁷⁸ She is not prohibited from purchasing stock by a statute providing that married women shall not be capable of making any contract to affect their real or personal estate, without the written consent of her husband, as the statute applies to executory contracts only.⁷⁹

We have seen in a former chapter that by the weight of authority in this country a corporation cannot purchase or subscribe for stock in another corporation. This is not because a corporation is incapable of making such a contract, but because it is generally not within the purposes for which it was created, and is, therefore, *ultra vires*. A corporation may be authorized by its charter to hold stock in other corporations.⁸⁰

A corporation cannot, in its own name, or in the name of others as trustees for it, subscribe for shares of its own stock.⁸¹

Municipal corporations are often expressly authorized to subscribe for stock in railroad corporations for the purpose of aiding them; but

⁷⁵ 1 Cook, Stock, Stockh. & Corp. Law, § 66; *National Commercial Bank v. McDonnell*, 92 Ala. 387, 9 South. 149; *Pugh and Sharman's Case*, L. R. 18 Eq. 566.

⁷⁶ That she may bind her separate estate by subscription, under the married woman's acts, see 1 Cook, Stock, Stockh. & Corp. Law, § 66.

⁷⁷ *Porter v. Bank of Rutland*, 19 Vt. 410; *Robinson v. Turrentine*, 59 Fed. 554; *Keyser v. Hitz*, 133 U. S. 138, 10 Sup. Ct. 290.

⁷⁸ *Robinson v. Turrentine*, *supra*.

⁷⁹ *Post*, p. 586.

⁸⁰ *Ante*, p. 151.

⁸¹ 1 Cook, Stock, Stockh. & Corp. Law, § 64; *Holladay v. Elliott*, 8 Or. 85; *Allibone v. Hager*, 46 Pa. St. 48.

they have no implied authority to subscribe for stock in any corporation.⁸²

There is nothing to prevent the directors and other officers and agents of a corporation from subscribing for its stock, if there is no fraud.⁸³

SAME—FORM OF SUBSCRIPTION—STATUTORY FORMALITIES.

99. At common law no formalities are necessary to a contract of subscription. By the better opinion it may be entered into verbally. But, where the statute or charter prescribes particular formalities, they must generally be followed.

At Common Law.

At common law no particular form is necessary to the validity of a contract of subscription, but all that is necessary is that an intention shall appear on the part of the subscriber to take stock and on the part of the corporation to recognize him as a stockholder. If such an intention appears, the fact that the writing is informal can make no difference.⁸⁴ The term "subscription" etymologically signifies writing; and some of the courts have held that writing is necessary to a valid contract of subscription.⁸⁵ By the better opinion, however, at common law, writing is not at all necessary. A contract of subscription, like other contracts, may be entered into verbally unless writing is required by the charter or by some statute.⁸⁶ Such a contract is not within the statute of frauds.⁸⁷

⁸² 1 Cook, Stock, Stockh. & Corp. Law, §§ 90-103.

⁸³ 1 Cook, Stock, Stockh. & Corp. Law, § 65; *Walker v. Devereaux*, 4 Paige (N. Y.) 229; *Sims v. Railroad Co.*, 37 Ohio St. 556.

⁸⁴ *Nulton v. Clayton*, 54 Iowa, 425, 6 N. W. 685. A subscription is not rendered invalid by a mistake in the name of the corporation, but the contract will operate in favor of the corporation for whose benefit it was intended. *Milford & C. Turnpike Co. v. Brush*, 10 Ohio, 111.

⁸⁵ *Fanning v. Insurance Co.*, 37 Ohio St. 339. In *Vreeland v. Stone Co.*, 29 N. J. Eq. 188, the court, in holding a verbal contract of subscription invalid, expressly bases the decision on the ground that the charter required writing.

⁸⁶ 1 Cook, Stock, Stockh. & Corp. Law, § 52; 1 Mor. Priv. Corp. § 54; York

⁸⁷ See the cases cited above.

Formalities Required by Statute.

If the general or special law under which a corporation is organized prescribes particular formalities, compliance with the law is generally essential to a valid contract of subscription, for the legislature has a right to fix a particular mode for entering into such a contract. As was said by Judge Campbell in a Michigan case, no person can obtain rights of membership in a corporation except in compliance with its charter or governing law, and, if that prescribes any conditions or special methods of becoming a member, the law is imperative. There may be cases of mutual dealing which will estop the parties, but no contract of subscription can be valid if not in conformance with the statute.⁸⁸

Thus, where the statute or charter requires subscriptions in writing, verbal subscriptions are invalid.⁸⁹ So, where the statute under which a corporation is formed requires the associates to organize the corporation, and subscribe formal articles of association, a person who signs preliminary subscription papers, but does not subscribe the articles of association, does not become a shareholder, and cannot be held liable to the corporation as a subscriber. In *Poughkeepsie & S. P. R. Co. v. Griffin*⁹⁰ the statute under which the plaintiff corporation was organized, after providing for the opening of books for subscriptions, declared that when a certain amount of stock should be subscribed, and a certain percentage paid thereon, the subscribers might meet and elect directors, and that thereupon they should subscribe articles of association, in which should be set forth certain matters, and that each subscriber to such articles should subscribe thereto his name and place of residence, and the number of shares taken by him. It then provided for filing the articles of association in the office of the secretary of state, and declared that thereupon the persons who should so subscribe, and

Park Bldg. Ass'n v. Barnes, 39 Neb. 834, 58 N. W. 440, W. D. Smith, Cas. Corp. 42, and *Shep. Cas. Corp.* 21; *Colfax Hotel Co. v. Lyon*, 69 Iowa, 683, 29 N. W. 780; *Bullock v. Turnpike Co.*, 85 Ky. 184, 3 S. W. 129; *Webb v. Railroad Co.*, 77 Md. 92, 26 Atl. 113; *Wemple v. Railroad Co.*, 120 Ill. 196, 11 N. E. 906. And see *Chaffin v. Cummings*, 37 Me. 76.

⁸⁸ *Carlisle v. Railroad Co.*, 27 Mich. 315, 318. See 1 Mor. Priv. Corp. § 67.

⁸⁹ *Vreeland v. Stone Co.*, 29 N. J. Eq. 188.

⁹⁰ 24 N. Y. 150.

such persons as should from time to time become stockholders, should be a body corporate. The defendant, with others, signed a paper, agreeing to take a certain number of shares of stock, but he did not subscribe the articles of association. It was held that he was not liable as a subscriber, as the statute contemplated subscriptions only by subscribing the articles of association, and the paper signed by him was merely a preliminary agreement for the purpose of bringing the parties together.⁹¹ So, where the statute provides that the persons desiring to organize a corporation should make, sign, and acknowledge the articles of association, one who signs, but does not acknowledge, them, does not become liable as a subscriber.⁹²

Same—Subscriptions after Incorporation.

This principle applies to subscriptions after incorporation as well as subscriptions prior to and in contemplation of incorporation. Sometimes the disposal of unsubscribed stock is left to the unrestricted discretion of the corporation, but this is not always the case. To prevent abuse, unfairness, and fraud, the charter or governing statute often prescribes the method of subscribing to stock in corporations after they have been organized; and, unless a subscription is in compliance therewith, the subscriber does not become a member of the corporation, and therefore is not liable on his subscription, in the absence of elements of estoppel. In *Carlisle v. Saginaw Val. & St. L. R. Co.*⁹³ the charter of the corporation declared that the persons who should subscribe the articles of association, and all other persons who should, from time to time thereafter, subscribe to or become the holders of the capital stock of said corporation, "in the manner to be prescribed by its by-laws," should be a body corporate. It was held that a subscription made after incorporation, but before any by-laws were adopted, gave no rights to either

⁹¹ And see *Troy & B. R. Co. v. Tibbits*, 18 Barb. (N. Y.) 297; *Dutchess & O. R. Co. v. Mabbett*, 58 N. Y. 397; *Sedalia, W. & S. Ry. Co. v. Wilkerson*, 83 Mo. 235; *Monterey & S. V. R. Co. v. Hildreth*, 53 Cal. 123. Compare, however, *Peninsular Ry. Co. v. Duncan*, 28 Mich. 130; *Greenbrier Industrial Exposition v. Rodes*, 37 W. Va. 738, 17 S. E. 305.

⁹² *Coppage v. Hutton*, 124 Ind. 401, 24 N. E. 112; *Greenbrier Industrial Exposition v. Rodes*, 37 W. Va. 738, 17 S. E. 305.

⁹³ 27 Mich. 315.

party, and, nothing having been done to operate as an estoppel, the subscriber was held not bound by a subsequent by-law adopting his subscription. So, as we shall see, if the statute or articles of association appoint or prescribe particular agents to receive subscriptions, no other person has authority to receive them, and a subscription received by another agent is not binding either on the corporation or on the subscriber.⁹⁴

Same—Directory Provisions.

The fact that the statute prescribes a particular way in which subscriptions may be received will not be held to render invalid subscriptions made in other ways, and good at common law, unless the intent of the legislature to make the designated mode exclusive is clear. Thus, where the statute under which a corporation was formed provided that when the articles of association should be filed as therein provided the directors named in the articles might, in case the whole capital stock should not be subscribed, open books of subscription to fill up the capital stock, it was held that the legislature did not intend to prohibit other modes of receiving subscriptions, and that a subscription which was good at common law was binding, though not received in the mode prescribed by the statute.⁹⁵

Same—Substantial Compliance with Statute.

Not every slight departure from the directions of the statute will render a subscription invalid. It is enough if there is a substantial compliance. Thus it has been held that, if the statute requires the directors to open books of subscription for the purpose of filling up the capital stock, it is a sufficient compliance with the provision if they adopt a book provided before the corporation was organized, and accept subscriptions, with the assent of the persons who made them, made and entered therein before organization. "The statute," it was said, "can mean no more than that the subscriptions are to be made in a book provided by the directors for that purpose, and, if they adopt one some one else has provided, every purpose of the

⁹⁴ Post, p. 293.

⁹⁵ Buffalo & J. R. Co. v. Gifford, 87 N. Y. 294. And see Stuart v. Railroad Co., 32 Grat. (Va.) 146.

statute is satisfied.”⁹⁶ So where the statute requires articles of association to be signed, setting forth the name of the corporation, its duration, and certain other matters, it has been held that it is sufficient if several separate papers, exact copies or transcripts of each other, setting forth the prescribed facts, are signed by the corporators, some signing one and some signing another of them. The several papers may be regarded as one instrument.⁹⁷

MUTUAL CONSENT.

100. Mutual consent on the part of the subscriber and of the corporation is essential to a valid contract of subscription.

No true contract can exist without mutual consent. This is true of contracts of subscription to the capital stock of a corporation. In the absence of elements of estoppel, no person can be held liable as a subscriber to the stock of a corporation unless he has consented to become a stockholder, and to become so in that corporation.⁹⁸

For this reason a person who subscribes to the stock of a corporation which it is proposed to form for a particular purpose, and with particular powers, does not become a shareholder, and is not liable on his subscription, if a corporation is formed by the other subscribers, without his consent, for a different purpose, or with different powers. In *Dorris v. Sweeney*,⁹⁹ the defendant signed a subscription paper for the formation of a corporation for the purpose of purchasing a patent “for preserving fruit or other products out of season,” erecting a building, and “stocking the same with fruits to be preserved.” Some of the subscribers organized a corporation under the general manufacturing act for “the manufacturing of preserved fruits, and the canning of fruits and other products, and the

⁹⁶ *Buffalo & J. R. Co. v. Gifford*, 87 N. Y. 294, 301. See *Woodruff v. McDonald*, 33 Ark. 97.

⁹⁷ *Lake Ontario, A. & N. Y. R. Co. v. Mason*, 16 N. Y. 451.

⁹⁸ *Dorris v. Sweeney*, 60 N. Y. 463; *Ticonic Water Power & Manuf'g Co. v. Lang*, 63 Me. 480; *Richmond Factory Ass'n v. Clarke*, 61 Me. 351; *Machias Hotel Co. v. Coyle*, 35 Me. 405.

⁹⁹ 60 N. Y. 463.

preserving and keeping of fruits and other articles from decay," etc. It was held that the defendant was not liable on his subscription, because the business of the company embraced branches in which he had never agreed to engage. So, in *Richmond Factory Ass'n v. Clarke*,¹⁰⁰ where a number of persons, including the defendant, signed an agreement to associate themselves together under a general law for the purpose of forming a manufacturing company, and the attorney general, to whom they had to apply under the law for a certificate, refused it, and some of those so subscribing, without the concurrence of the defendant, procured from the legislature a special act of incorporation to effectuate the purpose originally contemplated, it was held that the corporation so created could not enforce the defendant's original subscription.

On the same principle, where the subscription paper or the articles of association are materially altered without the consent of one of the subscribers thereto, he cannot be held liable on his subscription.¹⁰¹ And one who signs articles of association cannot be held liable as a subscriber if those articles are abandoned, and others substituted without his consent.¹⁰² So, where the certificate of incorporation varies materially from the preliminary subscription, a subscriber is not bound,—as where, by the subscription, the corporation should expire on a certain date, and the certificate fixes a much later date for expiration.¹⁰³

A subscription paper, to bind the subscribers, must be complete. Nothing must be left for further arrangement or consent. "A signature to an incomplete paper, wanting in any substantial particular, when no delegation of authority is conferred to supply the defect, does not bind the signer without further assent on his part to the completion of the instrument."¹⁰⁴ This applies to subscriptions. Therefore, where parties subscribed articles of association,

¹⁰⁰ 61 Me. 351.

¹⁰¹ *Burrows v. Smith*, 10 N. Y. 550; *Katama Land Co. v. Jernegan*, 126 Mass. 155.

¹⁰² *Southern Hotel Co. v. Newman*, 30 Mo. 118. See, also, *Richmond St. R. Co. v. Reed*, 83 Ind. 9.

¹⁰³ *Greenbrier Industrial Exposition v. Rodes*, 87 W. Va. 738, 17 S. E. 305. See, also, *Bucher v. Railroad Co.*, 76 Pa. St. 306.

¹⁰⁴ *Dutchess & C. C. R. Co. v. Mabbett*, 58 N. Y. 397.

leaving blank the spaces for the names of the directors, it was held that they were not bound as subscribers on the insertion of names of directors without their consent.¹⁰⁸

SUBSCRIPTIONS INDUCED BY FRAUD.

101. A subscription induced by the fraud of agents of the corporation authorized to solicit or receive subscriptions, or by unauthorized agents whose receipt of the subscription has been ratified by the corporation, is voidable at the option of the subscriber to the same extent, and subject to the same rules, as a contract between individuals would be. In detail:

(a) To constitute fraud—

(1) There must be a false representation or willful concealment of a material existing fact, and not a misrepresentation as to the law, nor mere expressions of opinion or promises. Representations as to the effect of the contract of subscription, or as to the rights and powers of the corporation under its charter, are as to matters of law, and do not vitiate the subscription.

(2) The representation must be made with intent to deceive.

(3) It must be relied upon, and must actually deceive.

(4) It must result in injury to the subscriber.

(b) Fraud renders the subscription voidable, and not void. Therefore

(1) The subscription cannot be avoided after it has been ratified. Receiving benefit from it, or acting as a stockholder with knowledge of the fraud, is a ratification.

¹⁰⁸ *Dutchess & C. C. R. Co. v. Mabbett*, 58 N. Y. 397. And see *McClelland v. Whiteley*, 15 Fed. 322.

(2) It cannot be avoided if the subscriber has been guilty of laches in discovering the fraud, or, after its discovery, in repudiating the contract.

So long as a corporation is a going concern, having the management and possession of its property, contracts made with it are governed by the same principles of law as contracts between individuals; and it is therefore well settled that if one is induced to become a subscriber to its capital stock by the fraud of the corporation or of its officers or agents, and within a reasonable time after discovery of the fraud, there having been no laches on his part in discovering it, repudiates his subscription before the company becomes insolvent, he is entitled to be relieved of all liability on his subscription; and the fact that the company subsequently becomes insolvent, and action is brought by its assignee or receiver, can make no difference.¹⁰⁶ And, though there are some cases to the contrary,¹⁰⁷ it is reasonable, and perhaps safe in most states, to say that, in the absence of statutory provisions to the contrary, if the fraud is not discovered until after the corporation becomes insolvent, and the subscriber has not been guilty of laches, he may even then avoid his subscription; for it cannot be said that under such circumstances the equities of creditors of the corporation are superior to those of the defrauded subscriber.¹⁰⁸

Authority of Agents.

It was at one time held in England that, if the agents of a corporation by false and fraudulent representations induce a person to subscribe for shares, this does not entitle the subscriber to avoid

¹⁰⁶ *Fear v. Bartlett*, 81 Md. 435, 32 Atl. 322, W. D. Smith, Cas. Corp. 58, and *Shep. Cas. Corp.* 26; *Savage v. Bartlett*, 78 Md. 561, 28 Atl. 414; *Vreeland v. Stone Co.*, 29 N. J. Eq. 188; *Ramsey v. Manufacturing Co.*, 116 Mo. 313, 22 S. W. 719; *Rockford, R. I. & St. L. R. Co. v. Shunick*, 65 Ill. 223; *Walker v. Railroad Co.*, 34 Miss. 245; *Directors, etc., of Central Ry. Co. of Venezuela v. Kisch*, L. R. 2 H. L. 99; *Crump v. Mining Co.*, 7 Grat. (Va.) 352; *Bradley v. Poole*, 98 Mass. 169; and cases hereafter cited.

¹⁰⁷ *Turner v. Insurance Co.*, 65 Ga. 649.

¹⁰⁸ *Ramsey v. Manufacturing Co.*, 116 Mo. 313, 22 S. W. 719; dictum in *Savage v. Bartlett*, 78 Md. 561, 28 Atl. 414.

the contract, nor give him a right of action against the corporation, but that his remedy is by action against the agents individually.¹⁰⁹ This view was based on the theory that the agents, in perpetrating the fraud, exceed their authority, and that the fraud therefore cannot be imputed to the corporation. These decisions have since been overruled, and it is now well settled, both in England and in this country, that, where the board of directors or other agents of a corporation, having authority to solicit or receive subscriptions for stock, induce a person to subscribe by false and fraudulent representations, the fraud is imputable to the corporation, and the subscriber may avoid his subscription.¹¹⁰ Some of the cases proceed on the theory that the representations are within the agent's apparent authority, while others proceed on the theory that the corporation cannot seek to reap the fruits of the contract without adopting the means by which it was obtained. If a person solicits subscriptions for a corporation without authority, and is guilty of fraud, the corporation, in afterwards ratifying his act in receiving the subscription, becomes bound by his fraud, and the subscription may be avoided.¹¹¹

What Constitutes Fraud.

The rules for determining what representations or concealment of facts constitute such fraud as will avoid a contract of subscription are the same as in the case of any other contract. "Contracts of this description between an individual and a company, so far as misrepresentation or suppression of truth is concerned, are to be treated like contracts between any two individuals. If one man makes a false statement, which misleads another, the way in which that is to be treated affords the example for the way in which a

¹⁰⁹ See note by Hon. Seymour D. Thompson in 14 Am. Law Rev. 177, 178; Holt's Case, 22 Beav. 48; Felgate's Case, 2 De Gex, J. & S. 456; Dodgson's Case, 3 De Gex & S. 85.

¹¹⁰ Note by Hon. Seymour D. Thompson, *supra*. See *Western Bank of Scotland v. Addie*, 5 Ct. Sess. Cas. (3d Series) 80; *Ranger v. Railway Co.*, 5 H. L. Cas. 72; *Directors, etc., of Central Ry. Co. of Venezuela v. Kisch*, L. R. 2 H. L. 99; *Crump v. Mining Co.*, 7 Grat. (Va.) 352; cases cited in note 106, *supra*, and in the following notes.

¹¹¹ *Walker v. Railroad Co.*, 34 Miss. 245.

contract is to be treated where a company makes a false statement, which misleads an individual.”¹¹²

Before going into details, it may be said, substantially in the language of Judge Chalmers in a Mississippi case,¹¹³ that, to avoid a subscription upon the ground of false representations by an agent of the corporation, it must appear that the statement was not made as an opinion, but as an ascertained and existing fact. It must not only be false in fact, but must also be either known to be so by the party uttering it, or his position must be one that made it his duty to know the truth. The resisting subscriber must show that he acted upon such statement; that his own position was such as warranted him in so acting; and that the statement was as to a fact material to the question of his subscription, and was relied upon by him. If the representations are as to matters controlled by the charter, and as to which the subscriber is bound to know that the agent has no right to make representations inconsistent therewith, they will not avoid the subscription. As to matters not controlled by the charter, false and fraudulent representations, which come within these limitations, and by which one has been entrapped into a subscription, will avoid the contract, just as fraud vitiates contracts of every character.

Fraud generally consists of a false representation of a material fact. But it must be borne in mind that concealment of facts may render a representation false.¹¹⁴ Thus, where a subscription to stock in a corporation was obtained by the representation that a prominent business man had subscribed for a large amount, but the fact that he had paid nothing for his shares was concealed, his subscription having been obtained for the express purpose of influencing others to subscribe, it was held that such concealment made the representation false and fraudulent, and was ground for avoiding the subscription.¹¹⁵

¹¹² Per Lord Romilly in *Directors, etc., of Central Ry. Co. of Venezuela v. Kisch*, L. R. 2 H. L. 99, 125.

¹¹³ *Selma, M. & M. R. Co. v. Anderson*, 51 Miss. 829.

¹¹⁴ *Clark*, Cont. 324.

¹¹⁵ *Coles v. Kennedy*, 81 Iowa, 360, 46 N. W. 1088, and *W. D. Smith, Oas. Corp.* 56. And see *Crump v. Mining Co.*, 7 Grat. (Va.) 352.

It is well settled that a misrepresentation of misunderstanding of the law will not vitiate a contract, where there is no misunderstanding of the facts. And this principle applies to subscriptions to the capital stock of a corporation as fully as to other contracts. It follows that misrepresentations by a corporation, or by its officers or agents, as to the legal effect of contracts of subscription to its stock, or as to the rights and powers of the corporation under its charter, though made for the purpose of inducing persons to subscribe, will not vitiate subscriptions, or constitute any defense in an action thereon, for such representations are as to a matter of law, subscribers being bound to take notice of the provisions of the charter, and of all general laws affecting the corporation, and of the terms and legal effect of subscription papers which they sign.¹¹⁶

Mere expressions of opinion or promises by the corporation or its officers or agents, though fraudulently made for the purpose of inducing a subscription, will not render the subscription voidable. The representation must be as to an existing fact. Thus it has been held that promises and representations as to what will be done by the corporation, and as to the advantages that will accrue to the subscribers, or as to the value of its assets and stock, or the holding out of flattering prospects, do not constitute such fraud as will vitiate a subscription induced thereby.¹¹⁷ So, false representations

¹¹⁶ *Upton v. Tribilcock*, 91 U. S. 45, 1 Cumming, Cas. Priv. Corp. 824. In this case the defendant had subscribed for shares in a corporation, and taken certificates, under which, by law, he became liable to assessment for the full amount of the shares. In an action on his subscription he set up fraud on the part of the agents of the corporation, relying upon false representations by them that 20 per cent. only of his subscription was required to be paid, and that 80 per cent. was nonassessable. It was held that these representations, being as to matter of law, were no defense. See, also, in support of the text, *Parker v. Thomas*, 19 Ind. 213; *Wight v. Railroad Co.*, 16 B. Mon. (Ky.) 4; *New Albany & S. R. Co. v. Fields*, 10 Ind. 187; *Ellison v. Railroad Co.*, 36 Miss. 572; *Clem v. Railroad Co.*, 9 Ind. 488. Compare *Wert v. Turnpike Co.*, 19 Ind. 242.

¹¹⁷ *Richelieu Hotel Co. v. International Military Encampment Co.*, 140 Ill. 248, 29 N. E. 1044, *W. D. Smith, Cas. Priv. Corp.* 48, *Shep. Cas. Corp.* 16; *Columbia Electric Co. v. Dixon*, 46 Minn. 463, 49 N. W. 244; *Walker v. Railroad Co.*, 34 Miss. 245; *Saffold v. Barnes*, 39 Miss. 399; *Hughes v. Manufacturing Co.*, 34 Md. 316, 326; *Armstrong v. Karshner*, 47 Ohio St. 276, 24 N. E. 897. Compare *Union Nat. Bank v. Hunt*, 76 Mo. 439.

in respect to such matters as the ability of a railroad company to construct the road, and the time within which it will be done, will not avoid a subscription to its stock.¹¹⁸

False representations, however fraudulently they may have been made, will never avoid a subscription, unless the subscriber believed in them, and relied upon them, so that his subscription was induced by them. This is a well-settled principle, applicable to all contracts, including subscriptions.¹¹⁹

On the other hand, it is also well settled that, where there has been fraudulent misrepresentation or willful concealment of facts, by which a person has been induced to enter into a contract, it is no answer to his claim to be relieved from it, that he might have known the truth by proper inquiry; and this principle applies where a subscription to stock is induced by fraud.¹²⁰

To render a representation fraudulent, and ground for avoiding a subscription, there must have been knowledge of its falsity, actual or imputable, and an intent to deceive.¹²¹

The rule that fraud must result in injury, in order to render a contract voidable, applies where a subscriber seeks to avoid his contract on the ground of fraud.¹²² In *Connecticut & P. R. Co. v. Bailey*¹²³ the defendant sought to defeat an action on his subscription to the stock of a corporation on the ground that subscriptions previous to his, and on the strength of which he was induced to subscribe, were fictitious, because of a secret agreement with the subscribers that they should not be called upon to pay. It was held that, as these subscribers were bound according to the expressed and absolute terms of their subscriptions, and could not avail themselves of the secret agreement, the fraud did not injure the defendant, and that he could not avoid his contract. It was also said that

¹¹⁸ *Bish v. Bradford*, 17 Ind. 490; *Parker v. Thomas*, 19 Ind. 213. See, also, *Wight v. Railroad Co.*, 16 B. Mon. (Ky.) 4; *Walker v. Railroad Co.*, 34 Miss. 245.

¹¹⁹ *Parker v. Thomas*, 19 Ind. 213; *Walker v. Railroad Co.*, 34 Miss. 245, 256.

¹²⁰ *Directors, etc., of Central Ry. Co. of Venezuela v. Kisch*, L. R. 2 H. L. 99.

¹²¹ *Salem Milldam Corp. v. Ropes*, 9 Pick. (Mass.) 187; *Goodrich v. Reynolds*, 31 Ill. 490.

¹²² *Connecticut & P. R. Co. v. Bailey*, 24 Vt. 465, W. D. Smith, Cas. Corp. 63, Shep. Cas. Corp. 28; *Anderson v. Railroad Co.*, 12 Ind. 376; *Keller v. Johnson*, 11 Ind. 337.

¹²³ 24 Vt. 465, W. D. Smith, Cas. Corp. 63, Shep. Cas. Corp. 28.

the different subscriptions were independent, and that the defendant had no right to rely on them.¹²⁴ For a like reason, where a note is given in payment of a subscription previously made, the subscription cannot be avoided because of false representations at the time the note was given.¹²⁵

Subscription Voidable and not Void—Ratification and Rescission—Laches.

It is well settled that a subscription induced by false and fraudulent representations is not absolutely void, but, like other contracts induced by fraud, is merely voidable at the option of the subscriber. It is valid until repudiated.¹²⁶ If the defrauded subscriber affirms the subscription after discovery of the fraud, he cannot afterwards repudiate it.¹²⁷ And he will be held to have affirmed it if it appears that, with knowledge of the fraud, he took part as an officer or as a shareholder in the management of the corporation, or paid assessments on his shares, or took any benefit from his shares.¹²⁸

To entitle a subscriber to be relieved from liability on his subscription on the ground that he was induced to subscribe by fraud,

¹²⁴ And see *Chouteau Ins. Co. v. Floyd*, 74 Mo. 286; *Blodgett v. Morrill*, 20 Vt. 509.

¹²⁵ *Goodrich v. Reynolds*, 31 Ill. 490.

¹²⁶ See *Upton v. Englehart*, 3 Dill. 496, Fed. Cas. No. 16,800; *Farrar v. Walker*, 3 Dill. 506, note, Fed. Cas. No. 4,679; and cases in the following notes.

¹²⁷ *City Bank of Macon v. Bartlett*, 71 Ga. 797.

¹²⁸ *City Bank of Macon v. Bartlett*, 71 Ga. 797; *Fear v. Bartlett*, 81 Md. 435, 32 Atl. 322, W. D. Smith, Cas. Corp. 58, Shep. Cas. Corp. 26. There may be circumstances under which a payment by the subscriber will not be held an affirmance. In *Fear v. Bartlett*, supra, it appeared that the defendant, who was unable to read or write, was induced by the fraud of a corporation to subscribe to its capital stock. Two months later he discovered the fraud, and immediately repudiated the contract. A year afterwards one of the directors came to the defendant, and told him he wanted to get \$10,000 to save the property of the company, and that he had paid \$5,000 in cash on account of his stock, and wanted to try and save what he had paid. To this the defendant replied that he would never give another dollar towards his subscription; but finally he said he was willing to give \$1,000 to save what he had already paid on his subscription, and thereupon he gave his check for that amount. It was held that under the circumstances, the defendant having testified that he did not intend a payment on his subscription, he should not be held to have affirmed his subscription.

he must have exercised care and vigilance to discover the fraud, and, having discovered it, he must have acted promptly in repudiating his contract. "A man must not," said Lord Romilly, "play fast and loose; he must not say, 'I will abide by the company if successful, and I will leave the company if it fails;' and therefore, whenever a representation is made, of which any one of the shareholders has notice, and can take advantage to avoid his contract with the company, it is his duty to determine at once whether he will depart from the company, or whether he will remain a member."¹²⁹

In England, under the companies act, a person who has been induced to subscribe to the stock of a corporation by fraud must not only repudiate the subscription within a reasonable time after discovery of the fraud, but he must take steps to have his name removed from the books of the company; and the proceedings to have his name removed must be instituted before the insolvency of the company. In the absence of a statute requiring this step on the part of the subscriber, it is held with us that removal of his name from the books of the corporation is not necessary to relieve a subscriber on the ground of fraud, but it is sufficient if he repudiates the subscription, and gives the company notice thereof.¹³⁰

SUBSCRIPTIONS UNDER MISTAKE.

102. If a person, without fault or negligence, signs a subscription paper under a mistake as to its nature, the subscription is not merely voidable, but void on the ground of mistake.

Fraud, as we have just seen, renders a subscription voidable. Mistake, on the other hand, renders a contract absolutely void. There are very few cases in which mistake can be set up to defeat a subscription. Perhaps it is safe to say that the only case is where the mistake was

¹²⁹ Ashley's Case, L. R. 9 Eq. 263, 268. And see Upton v. Tribilcock, 91 U. S. 45, 1 Cumming, Cas. Priv. Corp. 824; Ogilvie v. Insurance Co., 22 How. 380; Upton v. Englehart, 3 Dill. 496, Fed. Cas. No. 16,800; Farrar v. Walker, 3 Dill. 506, note, Fed. Cas. No. 4,679; Directors, etc., of Central Ry. Co. of Venezuela v. Kisch, L. R. 2 H. L. 99; City Bank of Macon v. Bartlett, 71 Ga. 797; American Building & Loan Ass'n v. Rainbolt (Neb.) 67 N. W. 493.

¹³⁰ Savage v. Bartlett, 78 Md. 561, 28 Atl. 414.

as to the nature of the transaction, and was induced by the deceit or other fault of the corporation or of some third party against which ordinary diligence could not guard.¹⁸¹ It has been said that: "If a person signs a subscription paper, entirely misunderstanding the nature of the instrument which he is signing, his subscription must be treated as null and void for want of mutual consent. In this case the question of fraud is not material."¹⁸² This is undoubtedly the law if the subscriber was not guilty of negligence in signing the paper.¹⁸³ If one should falsely read a subscription paper to a man who is unable to read, and he should sign it, without being guilty of negligence, the subscription would be void ab initio on the ground of mistake, and not merely voidable on the ground of fraud.¹⁸⁴

Subscriptions cannot be avoided because of a mistake as to the advantages to be gained by the incorporation. Thus it has been held that a subscription to a mill-dam corporation could not be avoided on the ground that the published estimate of the capacity of a mill was erroneous, and that the parties could not derive the expected benefits from the corporation, where there was no fraudulent intent to deceive those subscribing on the faith of the estimate.¹⁸⁵ Mistake of law can no more be set up as a defense in case of a subscription than in the case of any other contract.¹⁸⁶

SUBSCRIPTION BY AGENT.

103. A contract of subscription may be made by one person as agent for another, subject to the rules governing other contracts by agents. Some courts hold that one who assumes to subscribe as agent without authority does not himself become a stockholder, and so liable on the subscription, but is liable in damages for assuming to act without authority, while others hold him as a stockholder.

¹⁸¹ See Clark, Cont. 289, for the cases in which mistake renders a contract void.

¹⁸² 1 Mor. Corp. § 97.

¹⁸³ Clark, Cont. 291, 292.

¹⁸⁴ Rockford, R. I. & St. L. Co. v. Shunick, 65 Ill. 223.

¹⁸⁵ Salem Milldam Corp. v. Ropes, 9 Pick. (Mass.) 187.

¹⁸⁶ Clark, Cont. 305.

A contract of subscription, like any other contract, may be made by one person as agent for another, if he has authority, and, the subscription being accepted, and the shares apportioned to the agent for the principal, or to the principal, the latter becomes a stockholder as fully as if he had subscribed himself.¹³⁷ And where a person assumes to subscribe as agent for another without authority, the other may become a stockholder, and liable on the subscription by ratification.¹³⁸

It has been held by some of the courts that if a person subscribes another's name for shares in a corporation, without authority to do so, or where the other is not capable of subscribing, he thereby binds himself, and becomes a stockholder.¹³⁹ Other courts hold that he will be liable for damages in an action on the case for assuming to act without authority, but that he does not himself become a member of the corporation, and cannot be held liable on the subscription.¹⁴⁰ Ordinarily, it is immaterial that a subscription is made by an agent for an undisclosed principal; but such a subscription may be expressly or impliedly prohibited by the statute or charter. Thus, where an act incorporating a railroad company and appointing commissioners to open books and receive subscriptions required them, in case of subscriptions in excess of the capital stock, to distribute the stock among the subscribers in their discretion, and in a manner most advantageous to the company, it was held that, since the commissioners, to perform their duty, must know who the subscribers are, a subscription by an agent for an undisclosed principal, for the purpose of evading the statute, was prohibited and unlawful.¹⁴¹

¹³⁷ *Burr v. Wilcox*, 22 N. Y. 551. It is, of course, essential that authority be shown. See *McClelland v. Whiteley*, 15 Fed. 322.

¹³⁸ *Rutland & B. R. Co. v. Lincoln*, 29 Vt. 206. Declarations by the alleged principal to strangers, that he had taken the amount of stock subscribed for by the alleged agent, were held insufficient to show a ratification. *Rutland & B. R. Co. v. Lincoln*, *supra*. See, also, as to what constitutes ratification, *Ticonic Water-Power Manuf'g Co. v. Lang*, 63 Me. 480; *McClelland v. Whiteley*, 15 Fed. 322.

¹³⁹ *State v. Smith*, 48 Vt. 266, 284; *National Commercial Bank v. McDonnell*, 92 Ala. 387, 9 South. 149; *Allibone v. Hager*, 46 Pa. St. 48.

¹⁴⁰ *Salem Milldam Corp. v. Ropes*, 9 Pick. (Mass.) 187.

¹⁴¹ *Perkins v. Savage*, 15 Wend. (N. Y.) 412.

SAME—AGENTS TO RECEIVE SUBSCRIPTIONS.

- 104.** The person receiving a subscription to stock in a corporation that has been organized must be duly authorized, or the corporation must ratify his act, to render the subscription binding.
- 105.** If the charter, enabling act, or articles of association appoint particular agents to receive subscriptions, prior to or after organization, no other person has authority to receive them. They may, however, act by deputy.
- 106.** Agents appointed to receive subscriptions have such authority only as is conferred upon them; but unauthorized acts or stipulations may be ratified by the corporation.

Corporations can only contract by agent when the agent has been given authority to enter into the contract. A contract entered into by a person purporting to act as agent for a corporation, but who has not been given authority for the purpose, does not bind the corporation, and therefore does not bind the other party.¹⁴² This is true of subscriptions taken by a person without authority.¹⁴³ Such a subscription will become binding, however, if the corporation ratifies its receipt, and adopts it.¹⁴⁴

It often happens that the charter, or enabling act, or articles of association appoint or prescribe particular agents to receive subscriptions to the stock of a corporation which it is proposed to organize, or which has been organized. When this is the case, no other person has any authority to receive subscriptions. A subscription received by any other person is absolutely void. In *Shurtz v. Schoolcraft & Three Rivers R. Co.*¹⁴⁵ the articles of association of a railroad company, as provided by the general law under which it was formed, named five commissioners to open books for subscriptions to stock. The commissioners did not open books, but a subscription paper was circulated by an agent appointed by the board of directors, and the de-

¹⁴² Post, p. 493.

¹⁴⁴ Post, p. 500.

¹⁴³ *Essex Turnpike Corp. v. Collins*, 8 Mass. 292.

¹⁴⁵ 9 Mich. 269.

fendant subscribed thereon, and subsequently on several occasions promised to pay his subscription. It was held that the subscription was a nullity, and that the defendant was not liable on it.¹⁴⁶

It has been held that the receiving of subscriptions by commissioners appointed for that purpose is a ministerial act, since any one has a right to subscribe by complying with the statute, and that it may, therefore, be performed by an agent or deputy appointed by the commissioners, and that the commissioners may ratify a subscription received by one without authority.¹⁴⁷ But where the commissioners are required to distribute stock when more than the authorized amount has been subscribed, this power is a judicial one, being "a power to exercise a discretion founded on such considerations as may appear to them beneficial to the company's interests," and cannot be exercised by deputy. There being no provision that a majority shall constitute a quorum, all of the commissioners must be present to hear and consult, though a majority may then decide. A distribution at a meeting of less than all the commissioners is *coram non judice* and void.¹⁴⁸

Agents appointed to receive subscriptions, either before or after incorporation, have such authority only as is conferred upon them.¹⁴⁹ If they do unauthorized acts, or enter into unauthorized stipulations with subscribers, such acts or stipulations may become binding on the corporation by ratification or adoption, if within its powers.¹⁵⁰

SAME—CONDITIONAL SUBSCRIPTIONS.

107. A conditional subscription to stock of a corporation is a subscription to take effect only on the fulfillment of a condition precedent. The subscriber does not become a shareholder, nor liable on his subscription, until the condition is substantially performed according to its terms. When it is so performed, the subscription becomes absolute and unconditional.

¹⁴⁶ And see *Parker v. Railroad Co.*, 33 Mich. 23; *Northern Cent. Michigan R. Co. v. Eslow*, 40 Mich. 222.

¹⁴⁷ *Crocker v. Crane*, 21 Wend. (N. Y.) 211. And see *Penobscot R. Co. v. White*, 41 Me. 512.

¹⁴⁸ *Crocker v. Crane*, 21 Wend. (N. Y.) 211.

¹⁴⁹ Post, p. 493.

¹⁵⁰ Post, p. 500.

108. Conditional subscriptions after organization of a corporation are valid. Such subscriptions prior to and for the purpose of organization have also been sustained; but, by the better opinion, where it is proposed to organize a corporation under a charter or enabling act requiring a certain amount of stock to be subscribed, all subscriptions prior to organization must be absolute and unconditional. In some states, where a conditional subscription is made in such a case, the subscription is held void; but in others the condition only is void, and the subscription is valid.

109. Conditions precedent may be waived either by express agreement or by conduct showing such an intent.

By conditional subscription is meant a subscription the liability on which and the rights under which are dependent upon a condition precedent. Until the condition is fulfilled, no rights or liabilities at all arise out of the subscription. There is another class of subscriptions sometimes erroneously called "conditional subscriptions." These are absolute subscriptions on special terms. They are described by some writers and courts as subscriptions on conditions subsequent, but the better term is that applied by Mr. Morawetz, "subscriptions upon special terms."¹⁵¹ They are subscriptions which are absolute in so far as the liability thereon is concerned, and which make the subscriber a shareholder before compliance with the stipulations contained therein. The stipulations are merely terms of the contract of membership for the breach of which by the corporation the subscriber must resort to his remedy against it, as by action for damages.¹⁵² This class of subscriptions will be considered in the next section, and we will then see more at length the distinction between them and subscriptions upon conditions precedent, and the principles upon which it is determined whether a particular stipulation is a condition precedent or merely a special term.

¹⁵¹ 1 Mor. Corp. § 82 et seq.

¹⁵² Post, p. 302.

Subscriptions after Organization of the Corporation.

A person, in subscribing for stock in a corporation which has already been organized, has a right to make his subscription dependent upon the performance or fulfillment of a condition precedent, provided the corporation sees fit to accept such a subscription, and provided such subscriptions are not expressly or impliedly prohibited by its charter. In other words, he has a right to agree with the corporation that he will take stock and become a shareholder when a certain thing happens or is done. To allow such subscriptions after the corporation has been organized is not contrary to public policy. In such a case the subscriber does not become a shareholder, and therefore is not entitled to the rights nor subject to the liabilities of a shareholder, until the condition is performed according to its terms. His subscription is merely an agreement, or, according to some opinions, an offer, to become a shareholder when the condition has been fulfilled. Upon its fulfillment, without any further act or assent on his part, he becomes a shareholder and is liable on his subscription.¹⁵³

Thus, where a subscription to stock in a railroad company is expressly made upon condition that the road shall be located upon a certain route, the location of the road upon that route is a condition precedent to any liability on the subscription. The subscriber does not become a shareholder at all until then, but when the road is so located the subscription becomes absolute and unconditional, and the subscriber becomes eo instanti a shareholder, with all the rights and privileges and subject to all the liabilities of the other shareholders.¹⁵⁴ So, a subscription to stock of a railroad company may be

¹⁵³ Taggart v. Railroad Co., 24 Md. 563; Webb v. Railroad Co., 77 Md. 92, 26 Atl. 113; Corey v. Morrill, 61 Vt. 598, 17 Atl. 840; Ashtabula & N. L. R. Co. v. Smith, 15 Ohio St. 328; Chase v. Railroad Co., 38 Ill. 215; Armstrong v. Karshner, 47 Ohio St. 276, 24 N. E. 897; Philadelphia & W. O. R. Co. v. Hickman, 28 Pa. St. 318; Caley v. Railroad Co., 80 Pa. St. 363; Hanover Junction & S. R. Co. v. Grubb, 82 Pa. St. 36; Montpelier & W. River R. Co. v. Langdon, 46 Vt. 284.

¹⁵⁴ McMillan v. Railroad Co., 15 B. Mon. (Ky.) 218; Henderson & N. R. Co. v. Lenvell, 16 B. Mon. 364; Taggart v. Railroad Co., 24 Md. 563; Baltimore & D. P. R. Co. v. Pumphrey, 74 Md. 86, 21 Atl. 559; New Albany & S. R. Co. v. McCormick, 10 Ind. 499; Parker v. Thomas, 19 Ind. 213. Such a condition only requires location of the road on the route designated. It does not require actual construction and completion of the road before calling for payment of

made upon condition that the road shall be put under contract for grading or construction between certain points,¹⁵⁵ or that it shall be completed in whole or in part, or completed and put in operation,¹⁵⁶ or that a contract shall be made for equipping and ironing it.¹⁵⁷ So a person may subscribe on condition that a certain amount of stock shall be subscribed. In such a case he does not become a shareholder, and is not liable on his subscription, until bona fide binding and absolute subscriptions to the amount specified and of the kind specified have been received; and, if some of the subscriptions relied upon to make up the required amount were conditional, it must be shown that the conditions have been performed, so that the subscriptions have become absolute.¹⁵⁸

As stated above, in the case of a subscription upon condition precedent, the condition must be performed before any liability on the subscription will attach. And it must be performed according to its terms, and within the time limited, or within a reasonable time,

subscriptions. *Miller v. Railroad Co.*, 40 Pa. St. 237. In New York it has been held that it is contrary to public policy to allow subscriptions to the capital stock of a railroad, turnpike, or other similar corporation, on condition that the road shall be located on a certain route, or that its station or depot shall be located at a particular point, as it was considered that the directors should be left free to so act in these respects as to best serve the interests of the public. They hold that such a subscription is void, and the subscriber does not become a shareholder on performance of the condition. *Butternuts & Oxford Turnpike Co. v. North*, 1 Hill (N. Y.) 518; *Ft. Edward & F. M. Plank-Road Co. v. Payne*, 15 N. Y. 583. Most courts, however, sustain such a condition, at least if the company is not restricted from also locating lines, stations, or depots along other routes, or at other points, or otherwise doing whatever the public convenience may require, and many of them sustain such conditions without qualification. See the cases cited above.

¹⁵⁵ *Connecticut & P. R. R. Co. v. Baxter*, 32 Vt. 805.

¹⁵⁶ *Paducah & M. R. Co. v. Parks*, 86 Tenn. 554, 8 S. W. 842; *Armstrong v. Karshner*, 47 Ohio St. 276, 24 N. E. 897; *Leshner v. Karshner*, 47 Ohio St. 302, 24 N. E. 882; *Webb v. Railroad Co.*, 77 Md. 92, 26 Atl. 113.

¹⁵⁷ *Brand v. Railroad Co.*, 77 Ga. 506, 1 S. E. 255.

¹⁵⁸ *Philadelphia & W. C. R. Co. v. Hickman*, 28 Pa. St. 318; *Union Hotel Co. v. Hersee*, 79 N. Y. 454; *Brand v. Railroad Co.*, 77 Ga. 506, 1 S. E. 255; *People's Ferry Co. v. Balch*, 8 Gray (Mass.) 303; *Troy & G. R. Co. v. Newton*, Id. 596; *New York Exchange Co. v. De Wolf*, 31 N. Y. 273; *post*, p. 308. Of course void subscriptions, like subscriptions at common law by married women, cannot be considered in determining whether the required amount has been sub-

where no time is specified.¹⁵⁹ A substantial performance, however, as is the case with other contracts, is sufficient.¹⁶⁰

In some of the cases it is said that a conditional subscription which the corporation is authorized to receive is a mere continuing offer until the condition is performed; that the condition must be performed to constitute an acceptance of it; and that until then it may be withdrawn.¹⁶¹ But other courts, more properly, it seems, hold that after acceptance or assent by the corporation to a conditional subscription, which it is authorized to take, the subscriber is bound until performance of the condition to await such performance; that he cannot withdraw the subscription unless the performance is unreasonably delayed.¹⁶² If performance of the condition is unreasonably delayed, he may withdraw,¹⁶³ or perhaps the subscription would lapse without express withdrawal.¹⁶⁴ If a time is specified for performance of the condition, the subscription will lapse, and become void, if it is not performed within that time.¹⁶⁵

A conditional subscription, which is not a present valid contract, because the corporation has no authority at the time it is made to accept conditional subscriptions, will constitute a continuing offer to subscribe upon the specified conditions; and when those conditions are performed, if the offer be not before withdrawn, it will become an absolute and unconditional subscription.¹⁶⁶ The difference between such a subscription and a conditional subscription which the corporation is authorized to receive is that the former becomes a binding

scribed. *Hahn's Appeal* (Pa.) 7 Atl. 482. Where the condition of a subscription to stock of a railroad company is that, in the judgment of the directors, a sufficient amount be subscribed to build the road, the condition is performed when the board of directors in good faith pass a resolution that sufficient stock has been subscribed, though they may be mistaken. *Cass v. Railway Co.*, 80 Pa. St. 31.

¹⁵⁹ *Ticonic Water Power & Manuf'g Co. v. Lang*, 63 Me. 480.

¹⁶⁰ 1 Cook, Stock, Stockh. & Corp. Law, § 86; *O'Neal v. King*, 3 Jones (N. C.) 517.

¹⁶¹ *Webb v. Railroad Co.*, 77 Md. 92, 26 Atl. 113.

¹⁶² *Armstrong v. Karshner*, 47 Ohio St. 276, 24 N. E. 897.

¹⁶³ See *Stevens v. Corbitt*, 33 Mich. 458.

¹⁶⁴ See *Blake v. Brown*, 80 Iowa, 277, 45 N. W. 751.

¹⁶⁵ *Ticonic Water Power & Manuf'g Co. v. Lang*, 63 Me. 480.

¹⁶⁶ *Armstrong v. Karshner*, 47 Ohio St. 276, 24 N. E. 897.

contract when accepted, though the subscriber does not become a shareholder, nor liable as such, until the condition is performed, while the latter does not become binding until the condition is performed, and may, at any time before then, be withdrawn.¹⁶⁷

Subscriptions Prior to Incorporation.

Subscriptions upon conditions precedent, made prior to procuring a special charter, or prior to the organization of the corporation under a general law, have been sustained in some cases.¹⁶⁸ But the validity of such subscriptions is very doubtful, for they allow individuals to obtain charters from the government on subscriptions which may never become binding. Furthermore, they may operate as a fraud upon other persons who subscribe absolutely, and on the faith of the other subscriptions, and upon creditors who trust the corporation on the faith of such subscriptions.

It has been held, and may perhaps be regarded as established law, that where the charter or enabling act, under which it is proposed to organize a corporation, requires a certain amount of stock to be subscribed before corporate powers can be exercised, persons subscribing for stock prior to organization of the corporation, and for the purpose of organization, cannot attach conditions, but their subscriptions must be absolute and unconditional. The commissioners or other agents have no power to receive subscriptions dependent upon conditions precedent. As was said by the Pennsylvania court, "the commissioners who are appointed to receive subscriptions are not the accredited agents of the corporation, for it is not yet in being, but are rather the agents of the public, acting under limited and definite powers, which every one is bound to know; and, if he be misled by representations which such agents have no right to make, it is his own folly. Any other rule would lead to the procurement from the commonwealth of valuable charters without any absolute capital for their support, and thus give rise to a system of speculation and fraud which would be intolerable."¹⁶⁹ So, in *Burke v. Smith*,¹⁷⁰ it was said by Mr. Justice Strong, speaking of the invalidity of conditional

¹⁶⁷ *Armstrong v. Karshner*, *supra*.

¹⁶⁸ See *Montpelier & W. R. R. Co. v. Langdon*, 46 Vt. 284; *People's Ferry Co. v. Balch*, 8 Gray (Mass.) 303.

¹⁶⁹ *Caley v. Railroad Co.*, 80 Pa. St. 363.

¹⁷⁰ 16 Wall. 390.

subscriptions prior to organization of a railroad corporation: "When a company is incorporated under general laws, * * * and the law prescribes that a certain amount of stock shall be subscribed before corporate powers shall be exercised, if subscriptions, obtained before the organization was effected, may be subsequently rendered unavailable by conditions attached to them, the substantial requirements of the laws are defeated. The purpose of such a requisition is that the state may be assured of the successful prosecution of the work, and that creditors of the company may have, to the extent, at least, of the required subscription, the means of obtaining satisfaction of their claims. The grant of the franchise is, therefore, made dependent upon securing a specified amount of capital. If the subscriptions to the stock can be clogged with such conditions as to render it impossible to collect the fund which the state required to be provided before it would assent to the grant of corporate powers, a charter might be obtained without any available capital. Conditions attached to subscriptions, which, if valid, lessen the capital of the company, thus depriving the state of the security it exacted that the railroad would be built, and diminishing the means intended for the protection of creditors, are, therefore, a fraud upon the grantor of the franchise, and upon those who may become creditors of the corporation. They are also a fraud upon unconditional stockholders, who subscribed to the stock in the faith that capital sufficient would be obtained to complete the projected work, and who may be compelled to pay their subscriptions, though the enterprise has failed, and their whole investment has been lost. It is for these reasons that such conditions are denied any effect."

In New York it is held that a conditional subscription prior to such an incorporation is a nullity, and that no rights or liabilities at all can arise out of it.¹⁷¹ In Pennsylvania it is held that the condition only is void, and that the subscription is to be treated as absolute and unconditional.¹⁷²

¹⁷¹ *Troy & B. R. Co. v. Tibbits*, 18 Barb. (N. Y.) 297.

¹⁷² *Caley v. Railroad Co.*, 80 Pa. St. 363; *Boyd v. Railway Co.*, 90 Pa. St. 169; *Pittsburgh & S. R. Co. v. Biggar*, 84 Pa. St. 455; *Bavington v. Railroad Co.*, Id. 358.

Conditions must be Expressed in the Writing.

In Pennsylvania, because of the fact that the courts of law in that state have equitable jurisdiction, a written contract that is absolute on its face may be shown by parol evidence to have been conditional, and oral conditions precedent may be shown to defeat a recovery on a written subscription that is absolute on its face.¹⁷³ In most, if not in all, of the other states the rule excluding parol evidence to vary a written contract will render oral conditions void, and a condition, to have any effect, must be expressed in the writing.¹⁷⁴

Waiver of Condition Precedent.

Performance of a condition precedent in a subscription may be waived by the subscriber, and in such a case he cannot set up non-performance to escape liability on the subscription.¹⁷⁵ And the waiver may not only be by an express agreement, either oral or written, but it will be implied from any conduct on his part which clearly shows an intention not to insist upon the condition. Thus, in the absence of special circumstances negating an intent to waive a condition, a waiver will be implied if the subscriber, knowing, or with the means of knowing, that the condition has not been complied with, acts as a shareholder, or pays his subscription.¹⁷⁶

¹⁷³ See *Miller v. Railroad Co.*, 87 Pa. St. 95.

¹⁷⁴ 1 *Thomp. Corp.* § 1149; *Masonic Temple Ass'n of Minneapolis v. Channell*, 43 Minn. 353, 45 N. W. 716; *Wight v. Railroad Co.*, 16 B. Mon. (Ky.) 4; *Fairfield County Turnpike Co. v. Thorp*, 13 Conn. 173.

¹⁷⁵ 1 *Thomp. Corp.* § 1336; *O'Donald v. Railroad Co.*, 14 Ind. 259; *Slipher v. Earhart*, 83 Ind. 173; *Chamberlain v. Railroad Co.*, 15 Ohio St. 225; *Hutchins v. Smith*, 46 Barb. (N. Y.) 235; post, p. 310.

¹⁷⁶ *Cornell's Appeal*, 114 Pa. St. 153, 6 Atl. 258; *Mack's Appeal* (Pa. Sup.) 7 Atl. 481. But see, contra, *Atlantic Cotton Mills v. Abbott*, 9 Cush. (Mass.) 423. The decision in this case is the result of the ruling in Massachusetts that a subscription raises no implied promise to pay, and that the express promise is collateral to it. That part payment of a subscription is a waiver of unperformed conditions precedent, see *Cornell's Appeal*, supra; *Mack's Appeal*, supra. Giving unconditional notes for the amount of a subscription is a waiver of a condition precedent in the subscription, if it appears from the dates on which they are payable, or from other circumstances, that performance of the condition was not intended to precede payment of the notes. *Keller v. Johnson*, 11 Ind. 337. But it is otherwise if the circumstances under which the notes were given do not show an intention to waive the condition. *Parker v. Thomas*, 19 Ind. 213.

SUBSCRIPTIONS UPON SPECIAL TERMS.

- 110.** Subscriptions upon special terms are absolute subscriptions, by virtue of which the subscriber becomes a shareholder, and liable on his subscription, without performance of the stipulations, the stipulations being merely terms of his contract of membership.
- 111.** Subscriptions upon special terms are valid except
- (a) Where the stipulations are ultra vires, or inconsistent with the charter or articles of incorporation.
 - (b) Where they operate as a fraud upon the other shareholders by subjecting the subscriber to lighter burdens, or giving him greater rights and privileges.
 - (c) Where they operate as a fraud upon the creditors of the corporation who contract with it on the faith of the capital stock being fully paid.
- 112.** Only the managing agents of a corporation—as the directors—have power to accept subscriptions on special terms, but they may adopt or ratify such subscriptions taken without authority by commissioners prior to incorporation, or by other agents.

The distinction between conditional subscriptions or subscriptions upon conditions precedent, which we have considered in the preceding section, and subscriptions upon special terms, or, as they are sometimes inaptly termed, subscriptions upon conditions subsequent, is a very important one. In the former, as we have seen, the subscriber does not become a shareholder at all, nor liable on his subscription, until the condition has been performed.¹⁷⁷ In the latter, liability on the subscription, and the right to membership, do not depend at all upon performance of the stipulations. The subscriber becomes a shareholder at once, with all the rights and liabilities of a shareholder, and the stipulations are merely terms of his contract of mem-

¹⁷⁷ Ante, p. 294.

bership, for the breach of which he must seek his remedy against the corporation.¹⁷⁸ In *Paducah & M. R. Co. v. Parks*¹⁷⁹ a subscription to stock in a railroad company provided that one-fourth should be paid when the road should be completed to a certain county line, the remainder "to be paid in four equal installments of four months as the work progresses through the county, provided the company establishes a depot on said road" at a certain point. It was held that completion of the road to the specified county line was a condition precedent to any liability on the subscription, being made so by express terms, but that the erection of the depot was an independent stipulation, and not a condition precedent to rights of membership and liability on the subscription. So, in *Red Wing Hotel Co. v. Friedrich*,¹⁸⁰ the defendants had subscribed for shares in a hotel company to be organized, the shares to be paid for at such times and in such amounts as the board of directors might from time to time require. The subscription provided that it was upon the condition that the hotel to be built by the company should be located on a certain block. It was held that the building of the hotel was not a condition precedent to the right of the corporation to assess the shares and collect the assessments, as it was evident that the parties intended that the hotel should be built with money realized on the subscriptions.¹⁸¹

Whether a particular stipulation in a subscription is a condition precedent or merely an independent stipulation or special term is purely a question of intention, and the intention is to be determined

¹⁷⁸ "A subscription on a condition subsequent contains a contract between the corporation and the subscriber whereby the corporation agrees to do some act, thereby combining two contracts,—one, the contract of subscription; the other, an ordinary contract of a corporation to perform certain specified acts. The subscription is valid, and enforceable whether the conditions are performed or not. The condition subsequent is the same as a separate collateral contract between the corporation and the subscriber, for breach of which an action for damages is the remedy." 1 Cook, *Stock, Stockh. & Corp. Law*, § 78, quoted with approval in *Morrow v. Steel Co.*, 87 Tenn. 262, 10 S. W. 495. And see 1 Mor. *Priv. Corp.* § 82.

¹⁷⁹ 86 Tenn. 554, 8 S. W. 842.

¹⁸⁰ 26 Minn. 112, 1 N. W. 827.

¹⁸¹ For other illustrations of special terms, as distinguished from conditions precedent, see *Johnson v. Railroad Co.*, 81 Ga. 725, 8 S. E. 531; *American Building & Loan Ass'n v. Rainbolt* (Neb.) 67 N. W. 493.

by considering, not only the words of the particular clause, but also the language of the whole contract, the situation of the parties, the nature of the act required, and the whole subject-matter to which it relates.¹⁸² The courts lean strongly towards holding stipulations to be special terms, rather than conditions precedent. While the validity of conditional subscriptions is too firmly established to be now questioned, the courts do not favor them, and they will not hold a stipulation to be a condition precedent unless the intention to make it so is clear. This is proper, for, if a subscriber desires to make his liability dependent upon the performance of stipulations by the corporation, it is very easy for him to do so in express terms.¹⁸³ A stipulation certainly can never be considered a condition precedent when it appears that it was contemplated that the subscriber should vote at stockholders' meetings, or otherwise act as a shareholder.¹⁸⁴ And clearly, when a subscription is conditioned that the money acquired therefrom shall be expended in a certain way, the stipulation is a special term, and not a condition precedent, for the money cannot be expended until it has been paid.¹⁸⁵

Validity of Subscriptions upon Special Terms.

A corporation has no authority to receive subscriptions upon special terms where the stipulations are beyond its powers, or inconsistent with the charter or articles of incorporation. This is clear, and does not require the citation of authorities. Nor has it the power to receive a subscription upon such terms as will operate as a fraud upon the other shareholders by subjecting the subscriber to lighter bur-

¹⁸² See *Lane v. Brainerd*, 30 Conn. 565; *Johnson v. Railroad Co.*, 81 Ga. 725, 8 S. E. 531.

¹⁸³ *Paducah & M. R. Co. v. Parks*, 86 Tenn. 554, 8 S. W. 842.

¹⁸⁴ 1 *Mor. Priv. Corp.* § 89; *Morrow v. Steel Co.*, 87 Tenn. 262, 10 S. W. 495, 501.

¹⁸⁵ *Henderson & N. R. R. v. Leavell*, 16 B. Mon. (Ky.) 358. In *Connecticut & P. R. Co. v. Bailey*, 24 Vt. 465, *W. D. Smith, Cas. Corp.* 63, *Shep. Cas. Corp.* 28, there was a requirement in the charter of a railroad company that it should, within a certain time, expend a given sum in the construction of its road. The court held that this was not a condition precedent to liability on subscriptions. It would have been the same had the provision been expressly incorporated in the subscription. "It would be extremely inconsistent," it was said, "to say that the corporation must expend that sum in the construction of its road, and at the same time deny the right and power of collecting their subscriptions for that purpose."

dens, or giving him greater rights and privileges, or as a fraud upon creditors of the corporation by withdrawing the capital. It is well settled, therefore, that an agreement between a corporation and a subscriber, by which the subscription is not to be payable, or is to be payable in part only, whether it be for the purpose of pretending that the stock is really greater than it is, or for the purpose of preventing the predominance of certain shareholders, or for any other purpose, is illegal and void, and cannot be interposed as a defense in an action on the subscription.¹⁸⁶ In these cases the stipulation itself only is void, and does not affect the subscription. The courts hold the subscriber to his subscription as if the unlawful agreement had not been made, as the only means of preventing fraud and protecting the other subscribers and creditors.¹⁸⁷

An agreement that a subscriber need not pay at all, or that he need pay part only of his subscription, is void as against creditors of the corporation, even though the corporation and all the other shareholders may be parties to it; but, if no rights of creditors intervene, and the subscription is not necessary to make up the amount of stock required by the charter, so that there is no fraud upon the state, the agreement is binding upon the corporation and the other shareholders.¹⁸⁸

Subject to the restrictions above stated, a corporation may accept subscriptions upon special terms. A railroad company may agree to build a depot at a certain place in order to procure subscriptions from the residents of that neighborhood.¹⁸⁹ It may be agreed that the

¹⁸⁶ *White Mountain R. Co. v. Eastman*, 34 N. H. 124; *Melvin v. Insurance Co.*, 80 Ill. 446; *Union Mut. Life Ins. Co. v. Frear Stone Manuf'g Co.*, 97 Ill. 537; *Hickling v. Wilson*, 104 Ill. 54; *Bates v. Lewis*, 3 Ohio St. 459; *Henry v. Railroad Co.*, 17 Ohio, 187; *Meyer v. Blair*, 109 N. Y. 600, 17 N. E. 228; *York Park Bldg. Ass'n v. Barnes*, 39 Neb. 834, 58 N. W. 440, W. D. Smith, Cas. Corp. 42, *Shep. Cas. Corp.* 21; *Northrop v. Bushnell*, 38 Conn. 498; *Burke v. Smith*, 16 Wall. 390; *Upton v. Tribilcock*, 91 U. S. 45, 1 Cumming, Cas. Priv. Corp. 824; *Robinson v. Railroad Co.*, 32 Pa. St. 334; *Connecticut & P. R. R. Co. v. Bailey*, 24 Vt. 465, W. D. Smith Cas. Corp. 63, *Shep. Cas. Corp.* 28; *Blodgett v. Morrill*, 20 Vt. 509. So, an agreement that a subscriber may withdraw the money paid for his shares, and cancel the subscription, is void. *Melvin v. Insurance Co.*, *supra*; *post*, p. 330.

¹⁸⁷ See the cases above cited.

¹⁸⁸ *Winston v. Brooks*, 129 Ill. 64, 21 N. E. 514.

¹⁸⁹ *Paducah & M. R. Co. v. Parks*, 86 Tenn. 554, 8 S. W. 842.

stock may be paid for in work or in materials, provided the work or materials are an equivalent in value.¹⁹⁰ "In general, subscriptions to the capital stock of a corporation may be conditional as to the time, manner, or means of payment, or in any other way not prohibited by statute, or the rules of public policy, and not beyond the corporate powers of the corporation to comply with."¹⁹¹

Who may Receive Subscriptions on Special Terms.

Only the managing agents of a corporation are authorized to receive subscriptions upon special terms. They cannot be received prior to incorporation by the commissioners appointed to receive subscriptions, unless such authority is expressly conferred upon them by the charter or articles of association.¹⁹² But a subscription upon special terms, received by such agents without authority, may, if not withdrawn, be treated as a continuing offer to the corporation, and will become binding if accepted by the managing agents after the corporation has been organized.¹⁹³ An agent to solicit subscriptions, appointed by the managing agents of a corporation after its organization, cannot accept subscriptions upon special terms unless authority to do so has been conferred upon him. If he does accept such a subscription, however, without authority, the managing agents may ratify his act, and render the subscription binding.

CONDITIONAL DELIVERY OF SUBSCRIPTION.

113. If a subscription absolute in its terms is delivered in escrow, to take effect as a contract only upon the fulfillment of a condition—

- (a) It does not take effect until the condition is fulfilled, if the delivery was to a stranger, and not to the corporation or its agent, and the condition may be shown by parol evidence.
- (b) Most courts, perhaps, hold the rule to be the same where it was so delivered to the corporation or its agent; but some courts apply the rule governing deeds that there can be no delivery in escrow to

¹⁹⁰ Post, p. 379.

¹⁹¹ 1 Cook, Stock, Stockh. & Corp. Law, § 83.

¹⁹² 1 Mor. Corp. § 83.

¹⁹³ 1 Mor. Corp. § 86.

the other party or his agent, and that in such case the oral conditions are void, and the delivery absolute.

- (c) The subscriber may be estopped to set up the oral conditions to escape liability on his subscription, if others have subscribed and paid their subscriptions in the belief that his subscription was absolute, or if persons have contracted with the corporation in such belief.

A written subscription to stock, like other written instruments, may be delivered to some third person in escrow; that is, to take effect as a contract only on the happening of a contingency. In such a case it will not take effect until the condition is fulfilled. It is a well-settled rule that, to constitute a good delivery of a deed in escrow, the instrument must be delivered to some third person. If it is delivered to the other party or his agent, the condition is void, and the delivery absolute, for a delivery in fact outweighs verbal conditions.¹⁹⁴ Some courts have applied this rule to contracts not under seal, and have held that delivery of a written subscription to the agent of a corporation is an absolute delivery to the corporation. It has been so held where a subscription was delivered to the commissioners appointed to receive subscriptions,¹⁹⁵ and, it seems, where it was delivered to the promoter of a corporation, the promoter being regarded as the agent of the body of subscribers to take and hold subscriptions.¹⁹⁶ It has been held by most courts, however, that where a contract absolute in its terms is not under seal, it is admissible to show by parol evidence that it was delivered, even when delivered to the other party or his agent, with the understanding that it should not be operative as a contract from its delivery, but only on the happening of a contingency.¹⁹⁷ And in these jurisdictions the rule must apply to subscriptions as well as to other simple contracts.¹⁹⁸

Assuming that the rule last stated does apply to subscriptions, the

¹⁹⁴ Clark, Cont. 78, and cases there cited.

¹⁹⁵ Wight v. Railroad Co., 16 B. Mon. (Ky.) 4.

¹⁹⁶ Minneapolis Threshing-Mach. Co. v. Davis, 40 Minn. 110, 41 N. W. 1026.

¹⁹⁷ Westman v. Krumweide, 30 Minn. 313, 15 N. W. 255.

¹⁹⁸ Cass v. Railway Co., 80 Pa. St. 31.

doctrine of equitable estoppel may prevent the subscriber from setting up the defense to defeat an action on his subscription. According to this doctrine, where a person, by his words or conduct, willfully causes another to believe in the existence of a certain state of facts, and induces him to act on that belief, so as to alter his own previous condition, he is estopped from denying the truth of such facts to the prejudice of the other. It has been held, therefore, that where a person subscribes to the stock of a proposed corporation, and delivers the subscription to the promoter, or other agent, and other persons, without notice of any oral condition attached to such delivery, also subscribe to the stock, and pay the same in, and in reliance on the subscriptions the corporation is organized, engages in its business, expends large sums of money, and contracts liabilities therein, such person, when sued for installments due on his stock subscriptions, will not be allowed to defeat a recovery by showing that he attached a secret oral condition to the delivery of his subscription.¹⁹⁹

SUBSCRIPTION OF ENTIRE CAPITAL—DISTRIBUTION.

114. There is an implied condition that the whole amount of stock specified in the charter, articles of association, contract of subscription, or fixed by the incorporators or directors when authorized to settle the same, shall be actually taken by bona fide, binding, absolute, and unconditional subscriptions, before the subscribers shall be liable on their subscriptions. But

(a) The implication may be rebutted by the terms of the charter, articles of association, or contract of subscription.

(b) A subscriber may expressly or impliedly waive the condition.

115. Where stock is subscribed in excess of the authorized amount, and a distribution becomes necessary, the distribution is a condition precedent to liability on subscriptions.

¹⁹⁹ *Minneapolis Threshing-Mach. Co. v. Davis*, 40 Minn. 110, 41 N. W. 1028.

Where the charter or articles of association fix the amount of the capital stock of the corporation, there is generally an implied condition that the full amount shall be actually taken before the subscribers shall be liable on their subscriptions.²⁰⁰ The same implication arises where the contract of subscription fixes the amount of the capital stock.²⁰¹ And it arises where the amount is fixed by the incorporators or board of directors, when they are authorized to settle the same. In such a case the amount of stock must be settled and subscribed.²⁰² The rule also applies where the charter authorizes the corporation, when organized under a fixed capital, to increase it. When so increased, the amount fixed becomes the capital which must be subscribed before legal assessments can be made.²⁰³ The condition need not be expressed. It arises by im-

²⁰⁰ *Anderson v. Railroad*, 91 Tenn. 44, 17 S. W. 803, W. D. Smith, Cas. Corp. 53, Shep. Cas. Corp. 12; *Salem Milldam Corp. v. Ropes*, 6 Pick. (Mass.) 23; *Stoneham Branch R. Co. v. Gould*, 2 Gray (Mass.) 277; *Penobscot R. Co. v. Dummer*, 40 Me. 172; *Penobscot R. Co. v. White*, 41 Me. 512; *Denny Hotel Co. of Seattle v. Schram*, 6 Wash. 134, 32 Pac. 1002; *Connecticut & P. R. R. Co. v. Bailey*, 24 Vt. 465, W. D. Smith, Cas. Corp. 63, Shep. Cas. Corp. 28; *Hughes v. Manufacturing Co.*, 34 Md. 316, 331; *Bray v. Farwell*, 81 N. Y. 600; *New Hampshire Central Railroad v. Johnson*, 30 N. H. 390; *Read v. Gas Co.*, 9 Heisk. (Tenn.) 545; *Masonic Temple Ass'n of Minneapolis v. Channell*, 43 Minn. 353, 45 N. W. 716; *Anvil Min. Co. v. Sherman*, 74 Wis. 226, 42 N. W. 226; *Exposition Ry. & Imp. Co. v. Canal St. E. Ry. Co.*, 42 La. Ann. 870, 7 South. 627; *International Fair & Exposition Ass'n v. Walker*, 88 Mich. 62, 49 N. W. 1086; *Portland & F. R. Co. v. Spillman*, 23 Or. 587, 32 Pac. 688; *Hale v. Sanborn*, 16 Neb. 1, 20 N. W. 97.

²⁰¹ See *People's Ferry Co. v. Balch*, 8 Gray (Mass.) 303; *Troy & G. R. Co. v. Newton*, Id. 596; *Atlantic Cotton Mills v. Abbott*, 9 Cush. (Mass.) 423; *Union Hotel Co. v. Hersee*, 79 N. Y. 454; *Brand v. Railroad*, 77 Ga. 506, 1 S. E. 255; *Philadelphia & W. C. R. Co. v. Hickman*, 28 Pa. St. 318; ante, p. 297.

²⁰² *Anderson v. Railroad*, 91 Tenn. 44, 17 S. W. 803, W. D. Smith, Cas. Corp. 53, Shep. Cas. Corp. 12; *Troy & G. R. Co. v. Newton*, 8 Gray (Mass.) 596; *Proprietors of Cabot & West Springfield Bridge v. Chapin*, 6 Cush. (Mass.) 50; *Atlantic Cotton Mills v. Abbott*, 9 Cush. (Mass.) 423; *Haskell v. Worthington*, 94 Mo. 560, 7 S. W. 481; *Rockland, Mt. D. & S. Steamboat Co. v. Sewall*, 80 Me. 400, 14 Atl. 939.

²⁰³ *Read v. Gas Co.*, 9 Heisk. (Tenn.) 545. And see *Eaton v. Bank*, 144 Mass. 260, 10 N. E. 844; *Winters v. Armstrong*, 37 Fed. 508. In *Nutter v. Railroad Co.*, 6 Gray (Mass.) 85, a railroad company voted to issue 600 additional shares for the purpose of raising money to pay off indebtedness, and to allow each stockholder to take one new share for every two shares held by him, pro-

plication, says Mr. Cook, "from the just and reasonable understanding of a subscriber that he is to be aided by other subscriptions"; and "the rule is supported also by public policy, in that corporate creditors have a right to rely on the belief that the full capital stock of the corporation has been subscribed."²⁰⁴

The implication may be rebutted by the terms of the charter, articles of association, or contract of subscription, as where the corporation is authorized to commence business before the whole capital stock is subscribed.²⁰⁵ And a subscriber may expressly or impliedly waive the condition. A waiver will generally be implied if the subscriber consents to the letting of contracts, the creation of debt, or the doing of any corporate act involving the necessity of calling in the subscribed stock, unless the charter expressly forbids the doing of any corporate act until the requisite

provided he should, by a certain day, subscribe therefor, and pay a part of the amount, and give notes for the remainder. It was held that there was no implied condition that the whole 600 shares should be issued, and that the failure of the corporation to issue that amount was no ground for maintaining an action by a subscriber for some of such stock to recover back the money paid by him thereon, nor for defeating an action on the notes given by him.

²⁰⁴ 1 Cook, Stock, Stockh. & Corp. Law, § 176. And see *Stoneham Branch R. Co. v. Gould*, 2 Gray (Mass.) 277; *Denny Hotel Co. of Seattle v. Schram*, 6 Wash. 184, 32 Pac. 1002.

²⁰⁵ *Arkadelphia Cotton Mills v. Trimble*, 54 Ark. 316, 15 S. W. 776; *Schloss v. Trade Co.*, 87 Ala. 411, 6 South. 360; *Anderson v. Railroad Co.*, 91 Tenn. 44, 17 S. W. 803, *W. D. Smith, Cas. Corp.* 53, *Shep. Cas. Corp.* 12; *West v. Crawford*, 80 Cal. 19, 21 Pac. 1123; *Penobscot & K. R. Co. v. Bartlett*, 12 Gray (Mass.) 244; *Willamette Freighting Co. v. Stannus*, 4 Or. 261; *Astoria & S. C. R. Co. v. Hill*, 20 Or. 177, 25 Pac. 379; *Port Edwards, C. & N. Ry. Co. v. Arpin*, 80 Wis. 214, 49 N. W. 828. Where the corporation is authorized to begin business when a part of its capital stock is subscribed, subscription of that amount only is necessary before assessments can be made. *Schenectady & S. Plank-Road Co. v. Thatcher*, 11 N. Y. 102; *Boston, Barre & G. R. Co. v. Wellington*, 118 Mass. 79. And see the other cases cited in this note. In *Arkadelphia Cotton Mills v. Trimble*, 54 Ark. 316, 15 S. W. 776, the articles of association provided that "the capital stock of said corporation shall be \$50,000, of which \$14,500 has been subscribed, * * * and the residue may be issued and disposed of as the board of directors may from time to time order and direct." The company had begun business before the defendant subscribed for his stock. It was held that the implied condition that no subscription shall be payable until the whole capital stock is subscribed did not arise. And see *Nutter v. Railroad Co.*, note 203, *supra*.

stock is taken.²⁰⁶ So a waiver may be implied if a subscriber acts as a stockholder or officer of the corporation,²⁰⁷ or pays installments on his subscription, knowing that the entire capital stock has not been subscribed.²⁰⁸

It has been held that an assessment for the purpose of defraying preliminary expenses, as expenses incurred in obtaining the act of incorporation, and ascertaining the practicability and utility of the enterprise, is valid.²⁰⁹

It is almost too clear to require the citation of authority that subscriptions cannot be counted in order to make up the required amount, unless they are binding. Subscriptions, therefore, by married women, infants, and insane persons, which are void or voidable under the law of the particular jurisdiction, cannot be taken into consideration unless paid in.²¹⁰ Nor can ultra vires subscriptions by a corporation be considered.²¹¹ Unauthorized and unratified subscriptions by one as agent for another cannot be counted in those jurisdictions where it is held that the person assuming to act as agent does not himself become a shareholder.²¹² It is otherwise where, as in some states, it is held that he does himself become a

²⁰⁶ *Anderson v. Railroad Co.*, 91 Tenn. 44, 17 S. W. 808, W. D. Smith, Cas. Corp. 53, Shep. Cas. Corp. 12; *Hamilton v. Railroad Co.*, 144 Pa. St. 34, 23 Atl. 53; *Gibbons v. Ellis*, 83 Wis. 434, 53 N. W. 701. See *California Southern Hotel Co. v. Callender*, 94 Cal. 120, 29 Pac. 859.

²⁰⁷ *Masonic Temple Ass'n v. Channell*, 43 Minn. 353, 45 N. W. 716; *Cornell's Appeal*, 114 Pa. St. 153, 6 Atl. 258; *Auburn Opera-House & P. Ass'n v. Hill* (Cal.) 32 Pac. 587. There is no such waiver, however, from the fact that a subscriber, without knowledge that the requisite amount of stock had not been taken, on several occasions consented to and waived notice of stockholders' meetings, and on one occasion voted by proxy at a special meeting. *Portland & F. R. Co. v. Spillman*, 23 Or. 587, 32 Pac. 688. See *International Fair & Exp. Ass'n v. Walker*, 88 Mich. 62, 49 N. W. 1086.

²⁰⁸ See *Cornell's Appeal*, 114 Pa. St. 153, 6 Atl. 258.

²⁰⁹ *Salem Milldam Corp. v. Ropes*, 6 Pick. (Mass.) 28; *Central Turnpike Corp. v. Valentine*, 10 Pick. (Mass.) 142; *Anvil Min. Co. v. Sherman*, 74 Wis. 226, 42 N. W. 226.

²¹⁰ *Phillips v. Bridge Co.*, 2 Metc. (Ky.) 219; *Appeal of Hahn* (Pa.) 7 Atl. 482; ante, p. 275.

²¹¹ *Denny Hotel Co. v. Schram*, 6 Wash. 134, 32 Pac. 1002; ante, p. 151.

²¹² *Salem Milldam Corp. v. Ropes*, 9 Pick. (Mass.) 187; *California Southern Hotel Co. v. Russell*, 88 Cal. 277, 26 Pac. 105; ante, p. 291.

shareholder, and liable on the subscription.²¹³ Conditional subscriptions cannot be taken into consideration unless the conditions have been fulfilled, so that they have become absolute and unconditional; and the burden of showing this is on the corporation or creditors seeking to enforce the subscriptions.²¹⁴ Subscriptions by fictitious persons, or persons known to be insolvent, cannot be counted.²¹⁵ But apparent responsibility is all that can be required. A subscription cannot be avoided, nor an action thereon defeated, because of the financial irresponsibility of other subscribers for shares necessary to be subscribed, if the other subscriptions were taken in good faith from persons apparently responsible.²¹⁶ Whether a subscription upon special terms can be counted depends upon whether the terms reduce the amount to be paid upon the subscription below par, or for any other reason render the subscription invalid. If they do, they cannot be counted.²¹⁷ Some courts allow consideration of subscriptions entered into in good faith, payable in labor or materials, if the value of the labor or materials equals the amount of the subscription.²¹⁸ By the weight of authority, however, such subscriptions cannot be considered.²¹⁹

²¹³ See *State v. Smith*, 48 Vt. 266, 284.

²¹⁴ *Brand v. Railroad Co.*, 77 Ga. 506, 1 S. E. 255; *Oskaloosa Agr. Works v. Parkhurst*, 54 Iowa, 357, 6 N. W. 547; *Portland & F. R. Co. v. Spillman*, 23 Or. 587, 32 Pac. 688; *California Southern Hotel Co. v. Russell*, 88 Cal. 277, 26 Pac. 105; *Central Turnpike Corp. v. Valentine*, 10 Pick. (Mass.) 142.

²¹⁵ *Lewey's Island R. Co. v. Bolton*, 48 Me. 451. See *Denny Hotel Co. of Seattle v. Schram*, 6 Wash. 134, 32 Pac. 1002.

²¹⁶ *Penobscot R. Co. v. White*, 41 Me. 512; *Salem Milldam Corp. v. Ropes*, 9 Pick. (Mass.) 187. It is otherwise if the corporation treats such subscriptions as invalid, and ignores them. *Salem Milldam Corp. v. Ropes*, *supra*.

²¹⁷ See *New York Exchange Co. v. De Wolf*, 31 N. Y. 273; *Blodgett v. Morrill*, 20 Vt. 509. In *Rutland & B. R. Co. v. Thrall*, 35 Vt. 536, the full amount of stock was subscribed, but subscriptions contained a provision that interest should be paid by the corporation on all sums assessed and paid in, from the time of payment until the plaintiff's road should be put in operation. It was held that this provision did not amount to an agreement to pay back to the subscribers a part of the capital stock, so as to result in the whole stock not being subscribed.

²¹⁸ See *Phillips v. Bridge Co.*, 2 Metc. (Ky.) 219.

²¹⁹ 1 Cook, *Stock, Stockh. & Corp. Law*, § 180; *New York, H. & N. R. Co. v. Hunt*, 39 Conn. 75 (compare *Ridgefield & N. Y. R. Co. v. Brush*, 43 Conn. 86); *Troy & G. R. Co. v. Newton*, 8 Gray (Mass.) 596.

The fact that the full amount of capital stock has been subscribed may be shown by the records of the corporation, subject, of course, to rebuttal by evidence to the contrary.²²⁰ If the legislature has appointed commissioners to take subscriptions, and made it their duty, when the required amount is raised, to notify a meeting of subscribers for the organization of the corporation, and, after organization, to certify the fact to the secretary of state, the certificate of the commissioners showing that the required amount of stock was subscribed is conclusive, and a subscriber cannot defeat an action on his subscription by alleging that some of the subscriptions were not bona fide.²²¹

Excessive Subscription—Distribution.

If more than the authorized amount of stock is subscribed, so that a distribution becomes necessary in order to determine who are stockholders, and the number of shares each subscriber is entitled to, a distribution is necessary before a subscriber can be held liable.²²² In the distribution of stock the commissioners act judicially, and all must be present to hear and consult, though a majority may decide. A distribution at a meeting of less than all of them is coram non judice and void.²²³

PAYMENT OF DEPOSIT.

116. There is a conflict of opinion as to the effect of a failure to comply with a requirement in the charter or general law that a deposit, or percentage of each subscription, shall be paid at the time of subscribing.

²²⁰ Penobscot R. Co. v. Dummer, 40 Me. 172.

²²¹ Connecticut & P. R. R. Co. v. Bailey, 24 Vt. 465, W. D. Smith, Cas. Corp. 63, Shep. Cas. Corp. 28.

²²² Burrows v. Smith, 10 N. Y. 550. Such excessive subscription must be affirmatively shown, in an action on a subscription, in order to put the corporation to proof of a distribution; the presumption being that no more than the authorized amount was subscribed. Buffalo & N. Y. C. R. Co. v. Dudley, 14 N. Y. 336, 346.

²²³ Crocker v. Crane, 21 Wend. (N. Y.) 211.

(a) Where the subscription is prior to organization, it is held:

(1) In some states, that the provision is for the benefit of the public, and that noncompliance renders a subscription void.

(2) In other states, that the provision is for the benefit of the corporation, and may be waived by it, or that the subscriber cannot take advantage of his own wrong in failing to pay.

(b) Where the subscription is after incorporation, the provision will be construed as intended for the benefit of the corporation, unless the intention of the legislature to the contrary is clear, and non-compliance is no defense in an action on the subscription.

It is often provided, both in general laws authorizing the formation of corporations and in special charters, that a deposit, or a certain percentage of subscriptions, shall be paid at the time of subscribing. There is a direct conflict of opinion as to the object of this provision, and the authorities, therefore, do not agree as to the effect of a failure to comply therewith on subscriptions. Some courts have thought that the object in the case of subscriptions prior to organization, is to insure bona fide subscriptions, and "to prevent the subscription list from being filled with the names of nominal subscribers and the creatures of others,"²²⁴ and that the provision is intended not merely for the benefit of the corporation, but as a protection to the public, to prevent charters from being obtained fraudulently and by irresponsible persons. These courts hold that payment of the deposit in the case of subscriptions prior to incorporation is a condition precedent to the right of the subscriber to membership, and to his liability on his subscription; and that the condition, being imposed on grounds of public policy, and not merely for the benefit of the particular corporation, cannot be waived,

²²⁴ *President, etc., of Hibernia Turnpike Road v. Henderson*, 8 Serg. & R. (Pa.) 219, 228.

either by the commissioners appointed to receive subscriptions or by the corporation itself when organized.²²⁵ Other courts hold either that the provision is intended for the benefit of the corporation, and may therefore be waived by it, or that it is the duty of the subscriber to pay, and that he cannot take advantage of his own wrong in failing to do so; and they therefore hold that failure to pay the deposit, while it would give the corporation a right to refuse to recognize the subscription, does not render it void, and cannot be set up to defeat an action by the corporation or its creditors against the subscriber.²²⁶ Perhaps the former of these views is supported by the weight of authority. The latter seems the better sustained by reason. Of course, if the legislature clearly expresses the intention that there shall be no liability on the subscription if the deposit is not paid, the statute must be given this effect.

It would seem clear that a provision requiring payments by subscribers to the stock of a corporation that is already organized must be considered as intended for the benefit of the corporation only, and may be waived by it, and so it has been held.²²⁷ Where a statute appointed commissioners to open books and receive subscriptions, and provided that when a certain amount should be subscribed they should certify that fact to the governor, who should thereupon issue

²²⁵ *Jenkins v. President, etc.*, 1 Caines, Cas. (N. Y.) 86; *President, etc., of Highland Turnpike v. M'Kean*, 11 Johns. (N. Y.) 98; *Black River & N. R. Co. v. Clarke*, 25 N. Y. 208; *Beach v. Smith*, 50 N. Y. 116; *New York & O. M. R. Co. v. Van Horn*, 57 N. Y. 473; *President, etc., of Hibernia Turnpike Road v. Henderson*, 8 Serg. & R. (Pa.) 219; *Boyd v. Railway Co.*, 90 Pa. St. 169; *Taggart v. Railroad Co.*, 24 Md. 563.

²²⁶ *Wight v. Railroad Co.*, 16 B. Mon. (Ky.) 4, citing *President, etc., of Union Turnpike Road v. Jenkins*, 1 Caines (N. Y.) 381, which was reversed in *Jenkins v. President, etc.*, 1 Caines, Cas. (N. Y.) 86; *Illinois River R. Co. v. Zimmer*, 20 Ill. 654, relying on *Wight v. Railroad Co.*, *supra*; *Stuart v. Railroad Co.*, 82 Grat. (Va.) 146, 166 (where no reasons are given nor authorities cited); *Henry v. Railroad Co.*, 17 Ohio, 187 (dictum); *Minneapolis & St. L. Ry. Co. v. Bassett*, 20 Minn. 535 (Gil. 478). Compare *Vermont Cent. R. Co. v. Claves*, 21 Vt. 80 (distinguished in *Taggart v. Railroad Co.*, 24 Md. 563).

²²⁷ This distinction was expressly recognized in *Taggart v. Railroad Co.*, 24 Md. 563, and was so decided in *Oler v. Railroad Co.*, 41 Md. 593, and *Webb v. Railroad Co.*, 77 Md. 92, 26 Atl. 113. And see *Montpellier & W. R. R. Co. v. Langdon*, 46 Vt. 284. But see *Black River & U. R. Co. v. Clarke*, 25 N. Y. 208, and the other New York cases cited in note 225, *supra*.

letters of incorporation, it was held that a provision in that section of the statute requiring five dollars on each share to be paid the commissioners at the time of subscribing only applied to subscriptions received by the commissioners, and that the corporation, after organization, could receive subscriptions without such payment.²²⁸

Where payment of a deposit at the time of subscribing is required by the statute, payment not at the time, but subsequently, renders the subscription binding.²²⁹ So, where a person subscribed for stock on the understanding that the first installment of 10 per cent. required to be paid at the time of subscribing should be paid in subsequent services, and he subsequently claimed more for such services actually rendered than such installment, and the corporation paid him the balance, it was held that the subscription was binding.²³⁰ Payment is often expressly required to be made in money or cash, and, even in the absence of such an express requirement, the statute would be construed to mean payment in money or its equivalent. Payment by a note is not sufficient.²³¹ A check may be received for the deposit in the usual course of business, and, if presented and paid, will be a compliance with the statute;²³² but the commissioners cannot receive indorsed checks if it is known that the drawers have no funds, nor could a check be taken and held for the purpose of evading the statute.²³³ The deposit may be paid in services which the company has a right to contract and pay for, as this is equivalent to payment in cash.²³⁴

DELIVERY OF CERTIFICATE.

117. A certificate of stock, being merely evidence of the ownership of shares, is not necessary to make a subscriber a stockholder, with all the rights, and

²²⁸ Philadelphia & W. C. R. Co. v. Hickman, 28 Pa. St. 318. And see Southern Life Insurance & Trust Co. v. Lanier, 5 Fla. 110.

²²⁹ Black River & U. R. Co. v. Clarke, 25 N. Y. 208.

²³⁰ Beach v. Smith, 30 N. Y. 116.

²³¹ Boyd v. Railway Co., 90 Pa. St. 169. Compare Greenville & C. R. Co. v. Woodsides, 5 Rich. (S. C.) 145.

²³² Rothchild v. Hoge, 43 Fed. 97, 100.

²³³ Crocker v. Crane, 21 Wend. (N. Y.) 211.

²³⁴ Beach v. Smith, 30 N. Y. 116.

subject to all the liabilities, of stockholders. Nor is delivery or tender of a certificate necessary before action on a subscription, unless made so by the terms of the subscription.

A certificate of stock is merely evidence of the ownership of shares by the holder, and is not at all necessary to membership, even where issuance of certificates is required by the charter. In such a case, if the corporation refuses to issue a certificate to a subscriber, a court of equity might compel it to do so; but mere failure to issue or tender a certificate does not prevent a subscriber from becoming a shareholder, with all the rights, and subject to all the liabilities, of shareholders.²³⁵ Nor is the tender of a certificate necessary before bringing an action on a subscription.²³⁶ The parties may, however, expressly contract that the stock shall not be paid for until the certificate has been issued and delivered, and in such a case no action can be maintained by the corporation on the subscription until it has delivered or tendered a certificate.²³⁷ The rule that a certificate need not be delivered or tendered in order to maintain an action on a subscription does not apply to the case of a sale of stock, but such a contract stands on the same footing as a contract of sale of any other property.²³⁸

²³⁵ *Chester Glass Co. v. Dewey*, 16 Mass. 94; *Brigham v. Mead*, 10 Allen (Mass.) 245; *Wemple v. Railroad Co.*, 120 Ill. 196, 11 N. E. 906; *Walter A. Wood Harvester Co. v. Robbins*, 56 Minn. 48, 57 N. W. 317. W. D. S. 1000. *Cas. Corp.* 44; *Columbia Electric Co. v. Dixon*, 46 Minn. 463, 49 N. W. 244; *Beckett v. Houston*, 32 Ind. 393, 398; *Spear v. Crawford*, 14 Wend. (N. Y.) 20; *Rutter v. Kilpatrick*, 63 N. Y. 604; *Webb v. Railroad Co.*, 77 Md. 92, 26 Atl. 113; *New Albany & S. R. Co. v. McCormick*, 10 Ind. 499; *Miller v. Road Co.*, 52 Ind. 51; *Schaeffer v. Insurance Co.*, 46 Mo. 248; *Fulgam v. Railroad Co.*, 44 Ga. 597; *Chaffin v. Cummings*, 37 Me. 76; *Courtright v. Deeds*, 37 Iowa, 503; *Mitchell v. Beckman*, 64 Cal. 117, 28 Pac. 110.

²³⁶ Cases above cited.

²³⁷ See *Marson v. Deither*, 49 Minn. 423, 52 N. W. 38; *Courtright v. Deeds*, 37 Iowa, 503.

²³⁸ *Marson v. Deither*, 49 Minn. 423, 52 N. W. 38; *Summers v. Sleeth*, 45 Ind. 598; *Fulgam v. Railroad Co.*, 44 Ga. 597.

REMEDY OF CORPORATION ON SUBSCRIPTIONS.

118. In most states a subscription to the capital stock of a corporation implies a promise to pay assessments, upon which the corporation may maintain assumpsit. In Massachusetts and several other New England states an express promise must be shown.
119. A corporation has no inherent power to forfeit or sell shares upon nonpayment of assessments; but the power is almost always expressly conferred. The power must be exercised in strict accordance with the charter or statute, or the forfeiture or sale will be invalid.
120. The fact that the corporation is given the remedy by forfeiture does not prevent it from maintaining assumpsit. The remedies are cumulative.
121. A forfeiture releases the subscriber from further liability, but it is otherwise where the charter provides for a sale of the shares, and leaves the subscriber liable for any deficiency.

Action to Recover Assessments.

In several of the New England states, including Massachusetts, it is the settled doctrine that a mere subscription, or agreement to take shares in a corporation, though accepted and acted upon by the corporation after its organization, does not raise an implied promise on the part of the subscriber to pay assessments on the shares, so as to entitle the corporation to maintain assumpsit on the subscription; that to support such an action an express promise to pay must be shown; and that an agreement to take shares is not an express promise to pay assessments.²⁸⁹ In these states, in the absence of an ex-

²⁸⁹ Andover & Medford Turnpike Corp. v. Gould, 6 Mass. 40; Mechanics' Foundry & Machine Co. v. Hall, 121 Mass. 272; Katama Land Co. v. Jernegan, 126 Mass. 155; Franklin Glass Co. v. Alexander, 2 N. H. 380; dictum in Connecticut & P. R. R. Co. v. Bailey, 24 Vt. 465, W. D. Smith, Cas. Corp. 63, Shep. Cas. Corp. 28. But see Windsor Electric Light Co. v. Tandy, 66 Vt. 248, 29 Atl. 248.

press promise, the only remedy of the corporation is that given it by the statute, generally to forfeit, or forfeit and sell, the shares of delinquent shareholders. In most states the courts repudiate this doctrine, and it is held that the mere fact of subscription, where the subscription has been accepted by the corporation, raises an implied promise on the part of the subscriber to pay assessments, on the ground that there is a legal liability to pay them; and that, "whenever there is a legal liability, the law creates a promise upon which an action of assumpsit will lie."²⁴⁰ As we have seen, there is a sufficient consideration for the promise in the interest acquired by the subscriber in the corporate franchises and property, and the right to share in the profits.

Forfeiture and Sale of Shares.

A corporation has no inherent power to forfeit or sell the shares of stock of a delinquent shareholder for nonpayment of assessments. That is not a common-law remedy, and can only be exercised when it is expressly conferred by the charter, or by some statute, or by agreement of the stockholders.²⁴¹ The power, however, is almost always conferred either to sell the shares to pay overdue assessments, or to forfeit them to the use of the corporation. It cannot be conferred by a by-law unless it is expressly authorized.²⁴²

In declaring a forfeiture of stock for nonpayment of assessments, the corporation must adopt a course of proceeding reasonable and

²⁴⁰ *Instone v. Bridge Co.*, 2 Bibb (Ky.) 576; *Hughes v. Manufacturing Co.*, 34 Md. 816, 826; *Windsor Electric Light Co. v. Tandy*, 66 Vt. 248, 29 Atl. 248; *Dayton v. Borst*, 31 N. Y. 435; *Buffalo & N. Y. City R. Co. v. Dudley*, 14 N. Y. 336; *Rensselaer & Washington Plank-Road Co. v. Barton*, 16 N. Y. 457, note; *Spear v. Crawford*, 14 Wend. (N. Y.) 20; *Upton v. Tribilcock*, 91 U. S. 45, 1 Cumming, Cas. Priv. Corp. 824; *Griswold v. Trustees*, 26 Ill. 41; *Hartford & N. H. R. Co. v. Kennedy*, 12 Conn. 499, 506; *Danbury & N. R. Co. v. Wilson*, 22 Conn. 435; *Miller v. Road Co.*, 52 Ind. 51; *East Tennessee & V. R. Co. v. Gammon*, 5 Sneed (Tenn.) 566; *Bavington v. Railroad Co.*, 34 Pa. St. 358; *Dexter & Mason Plank-Road Co. v. Millerd*, 8 Mich. 91; *Carson v. Mining Co.*, 5 Mich. 288.

²⁴¹ *Budd v. Multnomah St. Ry. Co.*, 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60; *Minnehaha Driving Park Ass'n v. Legg*, 50 Minn. 333, 52 N. W. 898; *In re Long Island R. Co.*, 19 Wend. (N. Y.) 37. And see *Perrin v. Granger*, 30 Vt. 595.

²⁴² Post, p. 454.

just to the stockholder. Reasonable notice to him that his stock will be forfeited, unless by a specified time the overdue assessments are paid, is necessary to effect a forfeiture.²⁴³ In all cases the power to forfeit or sell must be exercised in the manner prescribed. A sale or forfeiture of shares without following the requirements of the charter or statute is just as invalid as if made without any power at all,²⁴⁴ and an invalid sale may constitute a conversion of the shares for which the corporation will be liable in damages.²⁴⁵ In *Budd v. Multnomah St. Ry. Co.*²⁴⁶ a statute provided that a corporation might make by-laws for the sale of stock for nonpayment of assessments, and it was held that a sale without a valid by-law authorizing it was invalid, and constituted a conversion of the shares. In this case the board of directors had passed a resolution ordering these particular shares to be sold, but it was held that this was not a by-law, because directed only against a particular shareholder.²⁴⁷ A sale of shares after a valid tender of the amount due for assessments is unauthorized and void, and a suit in equity may be maintained to set the same aside, and restrain a transfer of the shares to the purchaser.²⁴⁸ To authorize a forfeiture or sale of shares for nonpayment of assessments, the assessments must be valid. A sale for nonpayment of several assessments, one of which is invalid, is void.²⁴⁹ The measure of damages for conversion of shares by illegally selling them for nonpayment of assessments is not the full value of the shares, but their value less the amount of unpaid calls due thereon.²⁵⁰

If a corporation follows the provisions of its charter relating to the

²⁴³ *Rutland & B. R. Co. v. Thrall*, 85 Vt. 536; *Germantown Passenger Ry. Co. v. Fitler*, 60 Pa. St. 124.

²⁴⁴ *Budd v. Multnomah St. Ry. Co.*, 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60; *Portland, S. & P. R. Co. v. Graham*, 11 Metc. (Mass.) 1; *Germantown Passenger Ry. Co. v. Fitler*, 60 Pa. St. 124. As where a private sale is made, instead of a sale at public auction, as required by the statute. *Portland, S. & P. R. Co. v. Graham*, *supra*.

²⁴⁵ *Budd v. Multnomah St. Ry. Co.*, 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60.

²⁴⁶ 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60.

²⁴⁷ As to the validity of by-laws, see post, p. 454.

²⁴⁸ *Mitchell v. Mining Co.*, 67 N. Y. 280.

²⁴⁹ *Stoneham Branch R. Co. v. Gould*, 2 Gray (Mass.) 277.

²⁵⁰ *Budd v. Railway Co.*, 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60.

forfeiture of stock, its right to forfeit at the end of the time limited is perfect, and a stockholder who is in default can claim no further delay nor any other notice than that prescribed and given. When a forfeiture is regularly declared in accordance with the charter, equity will not relieve against it.²⁵¹

Action and Forfeiture as Cumulative Remedies.

The fact that the corporation is given the right to proceed against delinquent shareholders by forfeiture of their shares, or by forfeiture and sale of them, does not prevent it from maintaining assumpsit for assessments, either on an express promise, or on the implied promise which arises in most states. The statutory remedy is merely cumulative, unless it is clearly made exclusive, and the corporation may proceed in either way.²⁵²

Whether assumpsit can be maintained after resorting to the statutory remedy depends upon the nature of the statutory remedy. If, under the charter, the stock of a delinquent shareholder is merely forfeited to the use of the corporation,—that is, reclaimed by it to its own use,—on his failure to pay an assessment, the charter having, in effect, made the issue of the stock, not absolute, but in the nature of a conditional sale, the remedy by action is taken away.²⁵³ And when forfeiture is made an alternative, and not a cumulative, remedy, the same result follows.²⁵⁴ The reason is that such a forfeiture necessarily involves a total loss of interest in the thing forfeited by the party in default, and a resumption by the corporation of the entire consideration of the debtor's promise. The stock forfeited vests absolutely and beneficially in the company, and the debtor can have

²⁵¹ *Germantown Pass. Ry. Co. v. Fidler*, 60 Pa. St. 124.

²⁵² *Instone v. Bridge Co.*, 2 Bibb (Ky.) 576; *Worcester Turnpike Corp. v. Willard*, 5 Mass. 80; *Hartford & N. H. R. Co. v. Kennedy*, 12 Conn. 499, 506; *Goshen & M. T. Co. v. Hurin*, 9 Johns. (N. Y.) 217; *Buffalo & N. Y. City R. Co. v. Dudley*, 14 N. Y. 336; *Selma & T. R. Co. v. Tipton*, 5 Ala. 787; *Connecticut & P. R. Co. v. Bailey*, 24 Vt. 465, *W. D. Smith, Cas. Corp.* 63, *Shep. Cas. Corp.* 28; *Hightower v. Thornton*, 8 Ga. 486; *Hughes v. Manufacturing Co.*, 34 Md. 316, 326; *Tar River Nav. Co. v. Neal*, 3 Hawks (N. C.) 520, 535; *Grays v. Turnpike Co.*, 4 Rand. (Va.) 578, 583.

²⁵³ *Small v. Hydraulic Co.*, 2 N. Y. 330; *Mills v. Stewart*, 41 N. Y. 384; *Allen v. Railroad Co.*, 11 Ala. 437; *Rutland & B. R. Co. v. Thrall*, 35 Vt. 536.

²⁵⁴ *Edinburgh L. & N. Ry. Co. v. Hebblewhite*, 6 Mees. & W. 707; *Giles v. Hutt*, 8 Exch. 18; *Great Northern Ry. Co. v. Kennedy*, 4 Exch. 417.

no benefit from it or its proceeds, though the corporation might afterwards sell it for more than was due from him.²⁵⁵

Where, however, the security reserved by the charter to the corporation is less than forfeiture; where it is simply a power of sale to pay unpaid assessments, with the right reserved to the debtor to any surplus that may remain, so that the issue of the stock is absolute, and not conditional, and the security is in the nature of a mortgage or pledge,—a sale of stock for nonpayment of assessments does not take away the company's right of action, but it may maintain an action for a deficiency after applying the proceeds of the stock.²⁵⁶ An unsuccessful attempt to follow the remedy by forfeiture and sale could not bar an action to recover assessments. The shares not being sold, the liability of the shareholder on his promise would remain.²⁵⁷ In some charters it is expressly provided that, if the shares of a delinquent stockholder shall not sell for a sum sufficient to pay his assessments, with interest and charges of sale, he shall be held liable to the corporation for any deficiency. Of course, in such a case, a forfeiture and sale does not preclude an action for a deficiency.²⁵⁸

Not only does a forfeiture of shares by a corporation for nonpayment of assessments put an end to any liability of the shareholder to the corporation on his subscription, as shown above, but it relieves him from liability to existing or future creditors of the corporation if it becomes insolvent, provided there is no fraud or collusion.²⁵⁹ But a forfeiture by collusion between the shareholder and directors will not release him.²⁶⁰

CALLS.

122. If the time of payment of a subscription is fixed by the charter, statute, or subscription, no call is necessary to render the subscriber liable. But a call

²⁵⁵ In *Carson v. Mining Co.*, 5 Mich. 288. And see *Small v. Hydraulic Co.*, 2 N. Y. 330.

²⁵⁶ *Carson v. Mining Co.*, 5 Mich. 288.

²⁵⁷ *Instone v. Bridge Co.*, 2 Bibb (Ky.) 576.

²⁵⁸ *Danbury & N. R. Co. v. Wilson*, 22 Conn. 435, 456.

²⁵⁹ *Mills v. Stewart*, 41 N. Y. 384.

²⁶⁰ 1 Cook, Stock, Stockh. & Corp. Law, §§ 127, 128. See *Slee v. Bloom*, 19 Johns. (N. Y.) 456.

is essential to liability where it is expressly required by the charter, statute, or subscription, or, by the weight of authority, where the time of payment is left to the directors or stockholders. A call is not necessary after repudiation of the subscription.

123. Calls to be valid, must be made

- (a) In the manner prescribed.
- (b) By the person or board designated. If no person is designated, the power vests in the board of directors.
- (c) And it must operate uniformly upon all the shareholders.

124. When the charter or subscription requires notice of assessments, the requirement must be complied with; but, in the absence of any such requirement, notice is not necessary. Proof of actual notice obviates objections to the form or manner of the notice.

125. Interest runs on assessments from the time they are payable.

Necessity for Call.

Where, by the charter, statute, or terms of the subscription itself, the subscription is payable immediately, or where it is payable at a stated time or times, or within a certain time, and that time has elapsed, no call is necessary to render the subscriber liable to an action thereon.²⁶¹ Where, however, the contract of subscription, or the charter, or statute, or articles of association, or a valid by-law existing at the time of subscription, which always form a part of the contract of subscription, expressly make the subscription payable on call by the directors or majority of the stockholders, the subscription does not become payable, and no action can be maintained upon it, until a valid call is made in accordance with the provision; and by

²⁶¹ *Ruse v. Bromberg*, 88 Ala. 619, 7 South. 384; *New Albany & S. R. Co. v. Pickens*, 5 Ind. 247; *Phoenix Warehousing Co. v. Badger*, 67 N. Y. 294.

the weight of authority the same rule applies where the charter and contract of subscription are silent as to the time of payment.²⁶² In New York it is held, contrary to the weight of authority, that where the charter provides that the directors may require subscribers to pay the amount of their subscriptions "in such manner and in such installments as they may deem proper," and further provides for forfeiture of shares for nonpayment, the provision is designed to apply only to proceedings to forfeit shares, that the subscription is payable generally and unconditionally, and that no call is necessary before bringing suit on the subscription.²⁶³ No call is necessary after the subscriber has repudiated his subscription.²⁶⁴

²⁶² *North & S. St. R. Co. v. Spullock*, 88 Ga. 283, 14 S. E. 478; *Glenn v. Howard*, 65 Md. 40, 3 Atl. 895; *Ruse v. Bromberg*, 88 Ala. 619, 7 South. 384; *Seymour v. Sturgess*, 26 N. Y. 134; *Banet v. Railroad Co.*, 13 Ill. 504; *Spangler v. Railway Co.*, 21 Ill. 276. See *Williams v. Taylor*, 120 N. Y. 244, 24 N. E. 288. In *North & S. St. R. Co. v. Spullock*, *supra*, a contract of subscription provided that the subscription should be paid "in such installments and at such times as may be decided by a majority of the stockholders or board of directors, or a trustee empowered for the purpose by a majority of the stockholders." In a suit on the subscription it was not shown that the stockholders, directors, or trustee had ever provided in what installments the subscription should be paid, or fixed any time or times for such payment, or made any call for payment; and it was therefore held that a judgment of nonsuit was proper. In *Seymour v. Sturgess*, *supra*, the by-laws of a corporation declared that no call for stock should be made, except upon the vote and by the direction of at least five of the directors. It was held that one who became a subscriber after the enactment of the by-law was entitled to the benefit of it, as it constituted a part of his contract, and that there was no liability on his subscription in the absence of such a call. In *Glenn v. Howard*, *supra*, the question arose whether recovery on a call for an unpaid subscription, which, by the terms of the charter, was payable "as required by the president and directors," not made until after discharge of the subscriber in bankruptcy, was barred by such discharge. The court held that if the call had been made before the discharge, so as to become a debt provable in the bankruptcy proceedings, it would have been barred by the discharge, but that since there was no debt so provable before the call, and since the call was not made until after the discharge, it was not barred. Where it was provided that the directors might require payment of the sums subscribed at such times and in such proportions as they should deem best, but that no assessment should exceed \$10 on a share, it was held that the directors were not prevented from laying several assessments, not exceeding \$10 each, by one vote. *Rutland & B. R. Co. v. Thrall*, 35 Vt. 536.

²⁶³ *Lake Ontario, A. & N. Y. R. Co. v. Mason*, 16 N. Y. 451, 463.

²⁶⁴ *Cass v. Railway Co.*, 80 Pa. St. 31.

Validity of Call.

Assessments and calls for unpaid subscriptions, to be valid, must be made in a proper manner, and by the proper authority. If the charter or an authorized by-law prescribes a particular mode for making them, that mode must be followed. So if it specifies who shall exercise the power, the provision must be regarded, and a call or assessment made by any other authority will be ineffectual.²⁶⁵ Generally, the power is conferred upon the board of directors, and when this is the case it must be exercised by them, and in their official capacity as a board. By the weight of authority, they cannot delegate the power to others,²⁶⁶ but it has been held that they may ratify an exercise of the power by others.²⁶⁷ Sometimes the power is conferred upon the whole body of shareholders. If the charter is silent as to who shall exercise the power, it will devolve upon the directors, since they are the proper persons to perform such corporate acts.²⁶⁸

Where calls are required to be made by the board of directors, the board, to make a valid call, must be legally constituted.²⁶⁹ It is not enough that the call is made by directors de facto, for the rule that the acts of directors de facto cannot be questioned collaterally is only for the protection of third persons dealing with the corporation, and is not applicable as between the stockholders and the directors.²⁷⁰ To constitute a valid assessment, in the absence of any special requirement in the charter, all that is necessary is that there shall be some act or resolution of the directors, in their official capacity as a board, legally constituted, which shows a clear intention to render due and payable a part or all of the unpaid subscriptions.²⁷¹

²⁶⁵ *People's Mut. Ins. Co. v. Westcott*, 14 Gray (Mass.) 440; *Moses v. Tompkins*, 84 Ala. 613, 4 South. 763.

²⁶⁶ 1 Cook, Stock, Stockh. & Corp. Law, § 110; *Rutland & B. R. Co. v. Thrall*, 85 Vt. 536; *Silver Hook Road v. Greene*, 12 R. I. 164; *Banet v. Railroad Co.*, 13 Ill. 504.

²⁶⁷ *Rutland & B. R. Co. v. Thrall*, supra; *Read v. Gas Co.*, 9 Helsk. (Tenn.) 545.

²⁶⁸ 1 Cook, Stock, Stockh. & Corp. Law, § 109; *Budd v. Multnomah St. Ry. Co.*, 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60.

²⁶⁹ *People's Mut. Ins. Co. v. Westcott*, 14 Gray (Mass.) 440; *Moses v. Tompkins*, 84 Ala. 613, 4 South. 763.

²⁷⁰ *Moses v. Tompkins*, 84 Ala. 613, 4 South. 763; *People's Mut. Ins. Co. v. Westcott*, 14 Gray (Mass.) 440.

²⁷¹ *Budd v. Multnomah St. Ry. Co.*, 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60.

A call, to be valid, must operate uniformly upon all the shareholders. One of them cannot legally be required to pay in a larger proportion of his subscription, or to pay at an earlier day, than the others, unless his contract expressly permits it.²⁷² Of course, the existence of debts against the corporation is not necessary to a valid assessment.²⁷³ Where several assessments have been made, the directors may abandon or waive one that is void, and sue for those that are valid.²⁷⁴ The necessity for a call on unpaid subscriptions is to be determined by the board of directors, when the power to make calls is vested in them, and the propriety of their determination on this point cannot be questioned by the shareholders.²⁷⁵

A call cannot be made, except for preliminary expenses,²⁷⁶ until the corporation is sufficiently organized to enter upon the transaction of business, unless there is some express provision in the charter or contract of subscription authorizing it to be made before then, for until then it cannot be necessary. Thus, where a subscriber agreed to pay for his stock at such times and in such installments as the same might be called for by the corporation, and a statute declared that the corporation should not transact business until half of its capital stock should be subscribed, it was held that no call could be made until the condition of the statute should be fulfilled.²⁷⁷ It would be otherwise if no particular amount of stock were required to be subscribed before the corporation could begin operations.²⁷⁸

²⁷² *Great Western Tel. Co. v. Burnham*, 79 Wis. 47, 47 N. W. 373; *Pike v. Railroad Co.*, 68 Me. 445; 1 *Mor. Corp.* § 154; 1 *Cook, Stock, Stockh. & Corp. Law*, § 114. "But, if some shareholders," says Mr. Morawetz, "have already contributed more than others, it would be not only the right, but the duty, of the directors to make calls upon the other shareholders in such amounts as to equalize the contributions of all." 1 *Mor. Corp.* § 154.

²⁷³ *Penobscot R. Co. v. White*, 41 Me. 512.

²⁷⁴ *Read v. Gas Co.*, 9 Heisk. (Tenn.) 545.

²⁷⁵ *Budd v. Multnomah St. Ry. Co.*, 15 Or. 413, 15 Pac. 659, *W. D. Smith, Oas. Corp.* 60.

²⁷⁶ *Salem Milldam Corp. v. Ropes*, 6 Pick. (Mass.) 23; *Central Turnpike Corp. v. Valentine*, 10 Pick. (Mass.) 142; *Anvil Min. Co. v. Sherman*, 74 Wis. 226, 42 N. W. 226.

²⁷⁷ *Anvil Min. Co. v. Sherman*, 74 Wis. 226, 42 N. W. 226, collecting cases; *ante*, p. 808.

²⁷⁸ *Id.*

Notice and Demand.

Where the charter or subscription requires notice or demand as a condition precedent to suits to recover installments of stock, and there is no waiver of the condition, the prescribed notice must be given, or the prescribed demand made, or an action on a subscription cannot be maintained.²⁷⁹ But, in the absence of such a requirement, no notice or demand is necessary. The subscribers must take notice of the acts of the directors as to calls.²⁸⁰ Unless notice by publication is allowed by the charter or subscription, notice in a paper to which defendant is not a subscriber is not sufficient.²⁸¹ Nor would notice in any paper be sufficient unless it were shown that the subscriber read it, and so had actual notice. The fact that notice is not given in the way prescribed by the charter or statute, as by mail or publication, will not invalidate a call, if actual notice is shown. Proof of actual notice obviates all such objections.²⁸²

Interest.

An unpaid subscription bears interest from the time the subscriber is in default; that is, from the time he should pay the same. Where it is payable at once, and without call, interest commences to run at once. Where it is payable on call, interest runs from the time fixed for payment in the call.²⁸³ If notice of the assessment is required, interest runs, not from the date of the call, but from the time notice is given.²⁸⁴

²⁷⁹ Rutland & B. R. Co. v. Thrall, 35 Vt. 536; Banet v. Railroad Co., 18 Ill. 504; Spangler v. Railway Co., 21 Ill. 276.

²⁸⁰ Heaston v. Railroad Co., 16 Ind. 275.

²⁸¹ Lake Ontario, A. & N. Y. R. Co. v. Mason, 16 N. Y. 451, 463.

²⁸² Jones v. Sisson, 6 Gray (Mass.) 288; Schenectady & Saratoga Plank-Road Co. v. Thatcher, 11 N. Y. 102. And see Lexington & W. O. R. Co. v. Chandler, 13 Metc. (Mass.) 811.

²⁸³ Gould v. Town of Oneonta, 71 N. Y. 298. So, where the comptroller of the currency orders the receiver of a suspended national bank to collect unpaid subscriptions, interest runs from the date of the order. Casey v. Galli, 94 U. S. 678.

²⁸⁴ Hambleton v. Glenn, 72 Md. 831, 20 Atl. 115.

ASSIGNMENT OF UNPAID SUBSCRIPTION.

126. Where liability on a subscription has become fixed by a valid call, or where no call is necessary, it may be assigned by the corporation like any other debt.

Where the whole amount of an unpaid subscription has been regularly called in by the corporation, it stands like any other liquidated demand, in favor of the corporation, and the debt may be assigned by the corporation, even before judgment, to the same extent as it could assign any other debt.²⁸⁵ The assignment, in such a case, like all assignments of choses in action, is subject to equities, and cannot deprive the debtor of any rights as a stockholder which he would possess if no assignment had been made.²⁸⁶ Where a subscription is made payable without the necessity for a call, it may be assigned at any time.

RELEASE AND DISCHARGE OF SUBSCRIBER.

127. A subscriber may be released in whole or in part from his contract by the corporation with the consent of all the other shareholders; but he cannot withdraw and surrender his shares without the consent of the corporation; nor can he do so with the consent of the corporation, unless the other subscribers consent; nor can he do so with the consent both of the corporation and the other subscribers, if the amount due from him is required to pay corporate debts.

128. Violation of or noncompliance with its charter by a corporation, whereby its charter has become subject to forfeiture, does not release a subscriber.

²⁸⁵ Wells v. Rodgers, 50 Mich. 294, 15 N. W. 462.

²⁸⁶ Id.

- 129.** Alteration or amendment of the charter of a corporation by the legislature with the corporation's consent, will release a dissenting subscriber, except
- (a) Where the amendment is immaterial, as regards its effect on the contract between the subscriber and the corporation.
 - (b) Where it is authorized by a provision in the charter or in a general law.
- 130.** Abandonment of its business and franchises by a corporation will release a subscriber
- (a) If the abandonment is complete and final, and
 - (b) If no rights of creditors intervene.
- 131.** A subscriber is released by forfeiture of his stock to the corporation for nonpayment of assessments, but not by a sale of his shares to pay assessments, where, under the charter, he is liable for any deficiency.
- 132.** A subscriber is released by a valid transfer of his shares, whereby the transferee takes his place, and assumes his liability as a shareholder.

Withdrawal and Release—Reduction of Shares.

We have, in another place, considered the right of a subscriber to revoke or withdraw his subscription before it is accepted by the corporation, and we have seen that the right of revocation exists until such acceptance, except where the subscription is a step authorized by statute in the process of forming the corporation.²⁸⁷ We come now to the question whether a subscriber whose offer has been accepted by the corporation, so as to create a contract, can withdraw, and thereby avoid liability on his subscription. It is clear that he cannot do so without the consent of the corporation,—the other party to the contract. He cannot, merely by announcing his withdrawal, or withdrawal in part, from the company, and surrendering his shares, or some of them, absolve himself from liability or further liability on his subscription.²⁸⁸ It follows that an

²⁸⁷ Ante, p. 268. ²⁸⁸ Ante, p. 270; *Selma & T. R. Co. v. Tipton*, 5 Ala. 787.

assignment of his stock or a part of it to a fictitious person will not release him.²⁸⁹ And he cannot withdraw from his contract, or reduce his shares, even with the consent of the corporation, if the other subscribers do not consent; nor can he withdraw or reduce his shares by virtue of an agreement between him and the corporation, made at the time of subscribing, for the corporation has no power to make such an agreement with a subscriber either at the time of subscribing or afterwards. Such an agreement would be a fraud upon the other subscribers.²⁹⁰ A subscriber may, however, withdraw entirely, and surrender his shares, or reduce the number of shares subscribed for, with the consent both of the corporation and of the other shareholders, if in doing so he inflicts no injury upon the creditors of the corporation.²⁹¹ But he cannot be permitted to do so after debts have been incurred which there are no means to pay other than the capital stock subscribed, for the capital stock, as against creditors, cannot be squandered or given away.²⁹² And where a subscriber is sued by a creditor or receiver of the corporation on his original subscription, and claims in defense that the number of his shares was reduced, or that he withdrew, it is incumbent on him to show that it was at a time when it might lawfully be done.²⁹³ Even if a subscriber can claim a discharge on the ground that he offered to pay for his stock, and the officers of the corporation refused to receive payment, or to issue him a certificate, he cannot do so unless he treats it as a discharge. If he does not so treat it, but continues active in the company's business until it becomes insolvent, he will be liable.²⁹⁴

²⁸⁹ *Muskingum Valley Turnpike Co. v. Ward*, 13 Ohio, 120.

²⁹⁰ *Melvin v. Insurance Co.*, 80 Ill. 446; *White Mountain R. Co. v. Eastman*, 34 N. H. 124; *Hughes v. Manufacturing Co.*, 34 Md. 316, 330; *Gill v. Balis*, 72 Mo. 432; *Chouteau Ins. Co. v. Floyd*, 74 Mo. 286; *Cartwright v. Dickinson*, 88 Tenn. 476, 12 S. W. 1030; ante, p. 304.

²⁹¹ *Payne v. Bullard*, 23 Miss. 88.

²⁹² *Payne v. Bullard*, 23 Miss. 88; *Upton v. Tribilcock*, 91 U. S. 45, 1 Cumming, Cas. Priv. Corp. 824; *Webster v. Upton*, 91 U. S. 65; *Potts v. Wallace*, 146 U. S. 689, 13 Sup. Ct. 196; *Slee v. Bloom*, 19 Johns. (N. Y.) 456; *Phoenix Warehousing Co. v. Badger*, 67 N. Y. 294; *Bouton v. Dement*, 123 Ill. 142, 14 N. E. 62; post, p. 549.

²⁹³ *Payne v. Bullard*, 23 Miss. 88.

²⁹⁴ *Potts v. Wallace*, 146 U. S. 689, 13 Sup. Ct. 196.

Violation of Charter by Corporation—Mismanagement by Officers and Agents.

Failure of a corporation, after it has been organized, to comply with the provisions of its charter, or acts done in excess of its powers and in violation of its charter, whereby the charter has become subject to forfeiture at the instance of the state, cannot be set up by a shareholder to defeat an action on his subscription, either by the corporation itself or by its creditors, for, as has been shown in a previous chapter, it is exclusively for the state to determine whether it will exercise its prerogative of forfeiting or annulling the charter.²⁹⁵ Nor does the mere mismanagement of the affairs of the corporation by its officers and agents warrant the withdrawal therefrom of stockholders, and the repudiation of the obligations assumed by them as such.²⁹⁶ The shareholders' remedy in such cases is by suit for injunction,²⁹⁷ or, in a proper case, by suit to hold the officers who are guilty of the wrongful acts liable to the corporation.²⁹⁸

Alteration or Amendment of Charter.

It is well settled that an amendment of the charter of a corporation subsequent to subscriptions to its capital stock, whereby the objects and purposes of the corporation are materially enlarged or changed, will release from liability a subscriber who does not assent thereto, though the corporation and the other shareholders consent, unless the amendment was authorized by some provision in the charter or in the general laws.²⁹⁹ In *Proprietors of Union Locks and Canals v. Towne*,³⁰⁰ the original charter of a corporation em-

²⁹⁵ Ante, p. 237; *Mississippi, O. & Red River R. Co. v. Cross*, 20 Ark. 443; *Central Plank-Road Co. v. Clemens*, 16 Mo. 359; *Agricultural Branch R. Co. v. Winchester*, 13 Allen (Mass.) 29; *Little v. O'Brien*, 9 Mass. 423; *Taggart v. Railroad Co.*, 24 Md. 563; *Connecticut & P. R. R. Co. v. Bailey*, 24 Vt. 465, *W. D. Smith, Cas. Corp.* 63, *Shep. Cas. Corp.* 28; *Milford & Chillicothe Turnpike Co. v. Brush*, 10 Ohio, 111; *Cravens v. Mills Co.*, 120 Ind. 6, 21 N. E. 981.

²⁹⁶ *American Building & Loan Ass'n v. Rainbolt* (Neb.) 67 N. W. 493.

²⁹⁷ Ante, p. 164; post, p. 389.

²⁹⁸ Post, p. 389.

²⁹⁹ *Proprietors of Union Locks & Canals v. Towne*, 1 N. H. 44; *Hartford & N. H. R. Co. v. Croswell*, 5 Hill (N. Y.) 383; 1 *Cumming, Cas. Priv. Corp.* 894; *Middlesex Turnpike Corp. v. Locke*, 8 Mass. 268; ante, p. 204; post, p. 447.

³⁰⁰ 1 N. H. 44.

complete its road nor the nonuser of a part of it constitutes a defense to a suit on a subscription to its capital stock, unless such failure or nonuser violates some condition to that effect expressed in the subscription.³¹⁰ A shareholder is not released from liability for his unpaid subscription by the fact that the property and franchises of the corporation have been sold under foreclosure of a mortgage thereon, for the unpaid subscriptions continue part of the assets of the corporation for the benefit of all the stockholders and of creditors.³¹¹ Clearly, a sale of its property by a railroad company or other corporation, under a power conferred upon it by the provisions of its charter or of a law in force at the time of a subscription, does not release a subscriber, for such provisions form a part of his contract.³¹²

Forfeiture of Shares.

A subscriber, who has forfeited his shares for nonpayment of assessments, where the charter provides for a forfeiture, and not merely for a sale which will leave him liable for a deficiency, is released from any further liability, either to the corporation or to its creditors. Upon such a forfeiture he ceases to be a shareholder for any purpose. This question has been considered in a previous section.³¹³

Transfer of Shares.

Shares of stock are transferable by the holder without the consent of the other shareholders or of the corporation; and the effect of the transfer, provided it is valid, so that the transferee takes the transferror's place, and assumes his liability, is, in most jurisdictions, to release the transferror from any further liability as a shareholder. This question will be dealt with more at length in a subsequent section.³¹⁴

³¹⁰ *Armstrong v. Karshner*, 47 Ohio St. 276, 24 N. E. 897.

³¹¹ *Buffalo & J. R. Co. v. Gifford*, 87 N. Y. 294.

³¹² *Armstrong v. Karshner*, 47 Ohio St. 276, 24 N. E. 897.

³¹³ *Ante*, p. 319.

³¹⁴ *Post*, p. 409.

ESTOPPEL OF SUBSCRIBER.

133. A person who subscribes for stock in a corporation, and takes part in its organization or management, is generally estopped to deny the validity of his subscription.

We have seen in a previous chapter that one who subscribes for stock in a corporation after its organization or attempted organization is estopped to deny its corporate existence, and to say that it has not been legally organized, for the purpose of defeating an action on his subscription; since by contracting with the alleged corporation he admits its corporate existence.³¹⁵ We have also seen that this rule has no application to one who subscribes for stock previous to and in anticipation of incorporation, and who has not, by his subsequent acts, acquiesced in the mode of incorporation, but that in such a case it is an implied condition of his subscription that the proposed corporation shall be legally and regularly organized; and, if it is not, he may set it up as a defense to a suit on his subscription.³¹⁶ If, however, a subscriber to stock in a corporation to be formed takes active part in its organization, or in its management after organization, he cannot be heard to say that it was not legally organized when sued upon his subscription either by the corporation or by its creditors.³¹⁷ These questions all relate to estoppel to deny the legality of organization and existence of the corporation.

A subscriber may also be estopped to deny the validity of his subscription. It may be laid down as a general rule that one who subscribes for stock in a corporation, and takes part in its organization or management, cannot defeat an action on his subscription by showing that in subscribing he failed to comply with the formalities prescribed by the charter or by statute, or that the subscription was for any other reason invalid.³¹⁸

³¹⁵ Ante, p. 100, and note 43.

³¹⁶ Id.

³¹⁷ Id.

³¹⁸ *Selma & T. R. Co. v. Tipton*, 5 Ala. 737; *President, etc., of Centre & K. Turnpike R. Co. v. M'Conaby*, 16 Serg. & R. (Pa.) 140.

CHAPTER XL

MEMBERSHIP IN CORPORATIONS (Continued).

- 134. Right of Members to Inspect Books and Papers of Corporation.
- 135. Right to Vote at Meetings.
- 136-137. Profits and Dividends.
- 138-140. Increase of Capital Stock.
- 141. Shareholders' Right to Preference.
- 142-145. Preferred Stock.
- 146-148. Watered and Bonus Stock.
- 149-151. Action by Stockholders for Injuries to Corporation—Interference in Management.
- 152. Expulsion of Members.

RIGHT OF MEMBERS TO INSPECT BOOKS AND PAPERS OF CORPORATION.

134. A stockholder has the right to inspect the books and papers of the corporation, either personally or by an agent, provided he does so for a proper purpose, and at a proper time. And, if the right is denied him, it may be enforced by a writ of mandamus either to the corporation or to the custodian of the books and papers; or the stockholder may maintain an action for any damages sustained.

It is well settled in this country that any stockholder of a corporation is entitled to inspect the books and papers of the company for proper purposes and at proper times; and, if the right is wrongfully denied him by the corporation or its officers, he may maintain an action for any damages which he may have sustained thereby,¹ or he may enforce his right by petition for a writ of mandamus to compel the corporation or the officer having charge of the books and papers to permit an inspection,² or he may sue for the penalty

¹ Legendre v. Association, 45 La. Ann. 669, 12 South. 837.

² Lyon v. Screw Co., 16 R. I. 472, 17 Atl. 61; Huyler v. Cattle Co., 40 N. J. Eq. 392, 2 Atl. 274; People v. Throop, 12 Wend. (N. Y.) 183; Cockburn v. Bank,

where one is prescribed by statute.³ The writ may issue against the officer having the custody of the books, on his refusal to allow an inspection, and the corporation is not a necessary party.⁴

In the case of a partnership, every partner has an absolute and unrestricted right to examine the books and papers of the firm; but the right of stockholders of a corporation in this respect is not unlimited.⁵ By the weight of authority, at common law, the court will not issue a writ of mandamus to compel the corporation to allow an inspection, unless the petitioner shows some good reason for making an examination. The writ will not be issued to enable a stockholder to make an examination for the purpose of accomplishing purely personal or speculative ends, nor will it be issued "at the caprice of the curious or suspicious";⁶ but the petitioner must show a specific and a proper purpose.⁷ This rule, said the Rhode Island court, sufficiently protects the stockholder in all his substantial rights, and at the same time prevents an undue interference with the company in the conduct of its affairs. If a stockholder shows no good cause for a writ of mandamus, he is not injured by its refusal, and a company should not be hampered by frivolous and

13 La. Ann. 289; *Foster v. White*, 86 Ala. 467, 6 South. 88; *Stone v. Kellogg*, 62 Ill. App. 444.

³ *Lewis v. Brainerd*, 53 Vt. 519, *Shep. Cas. Corp.* 179, *W. D. Smith, Cas. Corp.* 86.

⁴ *Swift v. State*, 7 Houst. 338, 6 Atl. 856; *People v. Throop*, 12 Wend. (N. Y.) 183; *Foster v. White*, 86 Ala. 467, 6 South. 88; *State v. Bergenthal*, 72 Wis. 314, 29 N. W. 566.

⁵ See *Lyon v. Screw Co.*, *supra*.

⁶ *Com. v. Iron Co.*, 105 Pa. St. 111.

⁷ *Lyon v. Screw Co.*, *supra*; *People v. Lake Shore & M. S. R. Co.*, 11 Hun, 1, affirmed in *Re Sage*, 70 N. Y. 220; *Com. v. Iron Co.*, *supra*; *Phoenix Iron Co. v. Com.*, 113 Pa. St. 563, 6 Atl. 75; *State v. Einstein*, 46 N. J. Law, 479; *Appeal of Empire Pass. Ry. Co. (Pa.)* 19 Atl. 629. The right, said the Pennsylvania court, "is not to be exercised to gratify curiosity, or for speculative purposes, but in good faith, and for a specific, honest purpose, and where there is a particular matter in dispute, involving and affecting seriously the rights of the relator as a stockholder." *Phoenix Iron Co. v. Com.*, *supra*. In *Appeal of Empire Pass. Ry. Co.*, *supra*, it was held that mandamus would not lie to compel a corporation to allow a stockholder to make a list of the other stockholders, in order that they might be induced to join him in a suit which he proposed to institute against the corporation, and to share with him the expense of such suit.

vexatious demands by one who may have secured stock in hostility to its interests.⁹ A stockholder showing a prima facie case of fraud, and for the purpose of obtaining information to enable him to file a bill to obtain relief against the fraud, is entitled to an inspection.⁹ And the mere fact that he is hostile to and on bad terms with the officers of the corporation does not deprive him of the right.¹⁰ But a stockholder has no right of inspection where his purpose in making the examination is improper, or hostile to the interests of the corporation. Thus it has been held that not even a director of a corporation has the right to examine its letter files for the purpose of making memoranda for the benefit of a new and rival company in the organization of which he is interested, and that the secretary, in forcibly taking them from him, is not guilty of an assault and battery.¹¹

It has been said, in effect, that a stockholder is entitled to inspection, though his only object is to ascertain whether the affairs of the corporation have been properly conducted by the directors or managers, and that he need not first show that there has been mismanagement, or even that there are grounds for suspecting it.¹² By the better opinion, however, mere suspicion, without grounds therefor, does not entitle him to a writ of mandamus.¹³

The right of inspection need not be exercised by the stockholder personally; but may be exercised by an agent, as by a clerk, or an attorney, or an expert accountant. The right is personal in the sense that only a stockholder possesses and can enjoy it, but the in-

⁹ *Lyon v. Screw Co.*, *supra*.

⁹ *Phoenix Iron Co. v. Com.*, 113 Pa. St. 563, 6 Atl. 75.

¹⁰ *Huyler v. Cattle Co.*, 40 N. J. Eq. 392, 2 Atl. 274.

¹¹ *Hemingway v. Hemingway*, 58 Conn. 443, 19 Atl. 766.

¹² "Such a right is necessary to their protection. To say that they have the right, but that it can be enforced only when they have ascertained in some way without the books that their affairs have been mismanaged, or that their interests are in danger, is practically to deny the right, in the majority of cases. Oftentimes frauds are discoverable only by examination of the books by an expert accountant. The books are not the private property of the directors or managers, but are the record of their transactions as trustees for the stockholders." *Huyler v. Cattle Co.*, 40 N. J. Eq. 392, 2 Atl. 274, 278.

¹³ See cases cited in note 7, *supra*.

inspection and examination may be made by another for him; otherwise it would often be unavailing.¹⁴

Often the right of inspection is expressly given by statute, or by the charter or by-laws of the corporation, and under some provisions the right is broader than at common law. In Alabama the Code declares that "the stockholders of all private corporations have the right of access to, of inspection and examination of, the books, records, and papers of the corporation, at reasonable and proper times." There are similar statutes in other states. Under such a statute it was held by the Alabama court in a late case that any stockholder has an absolute right of inspection, subject only to the express limitation that the right shall be exercised at reasonable and proper times, and to an implied limitation that it shall not be exercised from idle curiosity, or for improper or unlawful purposes. In other respects the right is absolute. "The shareholder is not required to show any reason or occasion rendering an examination opportune or proper, or a definite or legitimate purpose. The custodian of the books and papers cannot question or inquire into his motives and purposes. If he has reason to believe that they are improper or illegitimate, and refuses the inspection on this ground, he assumes the burden to prove them as such."¹⁵

Sometimes, by statute, a corporation is made liable to a penalty for refusal to allow a stockholder to inspect its books, and officers or agents who are guilty of such refusal are subjected to a criminal prosecution. No damage need be shown to entitle a stockholder to recover the penalty, for it is imposed as a punishment for the violation of duty, and its recovery is not dependent upon any pecuniary loss.¹⁶

¹⁴ *Foster v. White*, 86 Ala. 467, 6 South. 88; *State v. Oil Works*, 28 La. Ann. 204.

¹⁵ *Foster v. White*, 86 Ala. 467, 6 South. 88. For other cases in which the right was expressly given, in absolute terms, by a statute, or by the charter or by-laws, see *Cotheal v. Brouwer*, 5 N. Y. 562; *People v. Steamship Co.*, 50 Barb. (N. Y.) 280; *State v. Bergenthal*, 72 Wis. 314, 39 N. W. 566; *Winter v. Baldwin*, 89 Ala. 483, 7 South. 734. The statute applies to national banks. *Winter v. Baldwin*, *supra*.

¹⁶ *Kelsey v. Fermentation Co.*, 51 Hun, 636, 3 N. Y. Supp. 723. The right to recover the penalty for such refusal is not waived by subsequently calling again, and making an examination. *Id.*

RIGHT TO VOTE AT MEETINGS.

135. A stockholder has a right to vote at corporate meetings.

This right will be considered at length when we come to treat of the management of the corporation, and of stockholders' meetings.

PROFITS AND DIVIDENDS.

136. A dividend is a fund which the corporation has set apart from its profits to be divided among its members.

137. The chief rules in relation to profits and dividends are as follows :

- (a) A stockholder has no legal right to a share of the profits of the corporate business until a dividend is declared.**
 - (b) But when a dividend is lawfully and fully declared, he acquires, as against the corporation, an absolute legal right to his share; and the declaration of the dividend cannot be revoked.**
 - (c) A dividend can lawfully be declared only out of the surplus or net profits. The capital cannot be distributed.**
 - (d) Whether a dividend shall be declared, even where there are profits, rests within the sound discretion of the directors; and they will be controlled in the exercise of this discretion at the suit of stockholders, only where they abuse it, and act fraudulently, oppressively, or unreasonably.**
 - (e) All who are stockholders at the time the dividend is declared are entitled to share therein in proportion to their stock, without regard to when the dividend was earned, or when they became stockholders; and the directors cannot discriminate between them.**
-

- (f) It is generally for the directors to determine how and when the dividend shall be payable.
 - (1) They may make it payable in money or in property. If no mode of payment is specified, it is payable in lawful money.
 - (2) They may pay it by issuing new stock, when authorized to increase the capital stock, and thus retain the surplus in the business. This is called a stock dividend.
- (g) The corporation may set off against his share of the dividend a debt due by the owner of stock at the time it is declared.
- (h) When a dividend has been declared,
 - (1) A stockholder may maintain assumpsit against the corporation as for money had and received.
 - (2) Or, in some cases, he may sue in equity.
 - (3) Demand is necessary before suit.
 - (4) Interest and the statute of limitations begin to run from the time of demand.
 - (5) Mandamus will not lie to compel payment.
- (i) Before a dividend has been declared
 - (1) No action, as for a debt, can be maintained by a stockholder to recover a share of the profits.
 - (2) But he may maintain a suit in equity to compel the corporation to declare and pay a dividend if it is wrongfully withheld.
 - (3) Mandamus is not a proper remedy.
- (j) If a dividend is wrongfully declared and paid, when there are no surplus profits,
 - (1) The directors are not personally liable to the corporation or to creditors in the absence of a statute, if they acted in good faith, and without negligence.
 - (2) But they are liable if they acted fraudulently or negligently.

(8) The property or funds wrongfully distributed may be followed and recovered by the corporation or by creditors in the hands of any one who is not an innocent purchaser or recipient for value.

If the business of a corporation is successful, and profits are realized, it sets apart from time to time, from these profits, a fund to be divided among its members in proportion to the amount of their shares. This fund is called a dividend. The term, as applied to corporate stock, has a technical, but well understood, meaning. It indicates "corporate funds derived from the business and earnings of the corporation, appropriated by a corporate act to the use of and to be divided among the stockholders."¹⁷ "Dividends" and "profits" are not synonymous terms. Dividends are paid out of the profits, but they can exist only where they have been declared or set apart by the directors out of the profits. Profits are not dividends until, as expressed in the above quotation, they are "appropriated by a corporate act" to be divided among the shareholders. In *Hyatt v. Allen*¹⁸ the plaintiff sold to the defendant stock in a corporation, reserving "all profits and dividends of and upon such stock" up to a certain time. A dividend having been partly earned before the time specified, but not declared until afterwards, it was held that the plaintiff was not entitled to any part of it under the reservation in the contract, for there was no dividend until it was declared.

Until dividends are declared, the surplus profits are part of the assets of the company, and do not belong to the stockholders individually, nor is there any debt due from the corporation to them, even though the circumstances are such that a dividend ought to be declared.¹⁹ It follows that, where a corporation becomes insolvent before its surplus fund has been set apart for the stockholders by declaring a dividend, the surplus, as well as the capital stock, must, if necessary, be applied to satisfy its debts, to the exclusion of any

¹⁷ *Hyatt v. Allen*, 56 N. Y. 553.

¹⁸ 56 N. Y. 553.

¹⁹ *Lockhart v. Van Alstyne*, 31 Mich. 76; *Beveridge v. Railroad Co.*, 112 N. Y. 1, 19 N. E. 489, 496; *Scott v. Fire Co.*, 7 Paige (N. Y.) 198; *Phelps v. Bank*, 26 Conn. 269; *Hill v. Mining Co. (Mo.)* 21 S. W. 508.

claim by the stockholders.²⁰ So, until a dividend has been declared, the stockholders cannot maintain an action against the corporation to recover their proportion of a surplus as a debt, their remedy being by suit in equity to compel the directors to declare and pay a dividend.²¹

It was said in an Alabama case that "dividends unpaid are assets of the company and liable for its debts,"²² but this is not true if the dividend has been declared and set apart. It is only true of surplus profits not set apart. When the directors of a corporation have lawfully declared a dividend from profits earned and received, the right of the stockholders to payment becomes vested, and there is a debt due them from the corporation; or, if money or other property equal to the amount of the dividend is specifically set apart as a fund appropriated to the payment of the dividend, the share of each stockholder therein is thereby severed from the common funds of the corporation, and becomes his individual property.²³ When a dividend is declared, the right of the stockholders thereto becomes vested, and the board of directors cannot afterwards, without their consent, revoke its action in declaring the dividend, and refuse to pay it.²⁴ Nor can insolvency of the corporation arising after the dividend has been declared and set apart defeat the right of the stockholders to their shares as against creditors.²⁵ To give the shareholders a vested right therein, the dividend must have been fully declared. Therefore it has been held in a late Massachusetts case that, where the fact that a dividend has been voted by the directors is not made public, nor communicated to the stockholders, and no fund is set apart for payment, the vote may be rescinded.²⁶

²⁰ *Scott v. Fire Co.*, 7 Paige (N. Y.) 198.

²¹ *Lockhart v. Van Alstyne*, 31 Mich. 76; *Beveridge v. Railroad Co.*, 112 N. Y. 1, 19 N. E. 489; post, p. 351, and cases there cited.

²² *Curry v. Woodward*, 44 Ala. 305.

²³ *Beers v. Spring Co.*, 42 Conn. 17; *King v. Railroad Co.*, 29 N. J. Law, 82; *Le Roy v. Insurance Co.*, 2 Edw. Ch. (N. Y.) 657; *In re Le Blanc*, 14 Hun (N. Y.) 8, 75 N. Y. 598; *Ford v. Thread Co.* 158 Mass. 84, 32 N. E. 1036; *Wheeler v. Sleigh Co.*, 39 Fed. 347, 2 Cumming, Cas. Priv. Corp. 203.

²⁴ *Beers v. Spring Co.*, 42 Conn. 17.

²⁵ *Le Roy v. Insurance Co.*, 2 Edw. Ch. (N. Y.) 657; *In re Le Blanc*, 14 Hun (N. Y.) 8.

²⁶ *Ford v. Thread Co.*, 158 Mass. 84, 32 N. E. 1036.

When Dividend May be Declared.

There are varying statutory or constitutional provisions in a number of states expressly restricting the right to pay dividends. Thus it is provided in some states that no dividend shall be paid except out of net profits properly applicable thereto, and which shall not in any way impair or diminish the capital; or except from surplus profits, arising from the business of the corporation; or if the payment of it will leave insufficient funds to meet the liabilities of the corporation, or will diminish the amount of its capital stock, etc. The object of these provisions is to prevent a corporation from paying dividends when there are no available funds, and to prevent it from impairing its capital by distributing any part of it among the stockholders. The statutes generally impose penalties on the directors for violating their provisions to which they are not liable at common law; but the principle upon which they are based, and the prohibition which they express, are fully recognized by the common law. Even at common law, dividends can lawfully be declared only out of the surplus or net profits.

The terms "net profits" or "surplus profits" mean that which remains as the clear gain of the corporation after deducting the capital invested, the expenses incurred, and the losses sustained.²⁷ As a rule, dividends cannot be declared out of borrowed money, for borrowed money is not profits;²⁸ but money might be borrowed temporarily for the purpose of paying dividends, if the corporation has used its current profits to make improvements for which it might have borrowed money.²⁹

"Profits" consist of earnings actually received. It has, therefore, been held that interest accrued, but not payable, and interest accrued, but not paid, though secured by safe mortgages, and drawing interest, are not "surplus profits," within the meaning of a statute prohibiting a corporation from paying dividends except from surplus profits.³⁰

²⁷ *Park v. Locomotive Works*, 40 N. J. Eq. 114, 3 Atl. 162; *Main v. Mills*, 6 Biss. 98, Fed. Cas. No. 8,974. See *Miller v. Bradish*, 69 Iowa, 278, 28 N. W. 594; *Hubbard v. Weare*, 79 Iowa, 678, 44 N. W. 915.

²⁸ *Davis v. Mining Co.*, 2 Utah, 74, 88.

²⁹ *Excelsior Water & Mining Co. v. Pierce*, 90 Cal. 131, 27 Pac. 44.

³⁰ *People v. San Francisco Sav. Union*, 72 Cal. 199, 13 Pac. 498.

The capital stock of an insurance company is not the primary fund for the payment of losses which may accrue upon existing risks, but premiums received for insurance and the interest on the capital stock constitute the primary and natural fund for the payment of the debts and losses of the company. Therefore the unearned premiums received by an insurance company on which the risks are still running are not surplus profits of the company, out of which dividends can be legally declared, without leaving a sufficient surplus on hand to meet the probable losses upon risks then assumed and not yet terminated, independent of the capital stock of the company.⁸¹

In deciding whether a dividend was rightfully or wrongfully made, the transaction must be viewed from the standpoint of that time, and not in the light of subsequent events. Notes or overdrafts, for instance, by persons then considered perfectly solvent, should not be considered as losses because they afterwards proved to be such.⁸²

The directors of a corporation cannot lawfully diminish the capital required to enable the corporation to do business, either by directly distributing a part of it among the stockholders, or by indirectly doing so by distributing funds as dividends when there are no surplus profits. It would be a fraud upon creditors of the corporation, who deal with it on the faith of its capital stock, to divert the same by distribution among the stockholders as a dividend.⁸³ Though a corporation may agree to pay interest on certificates of stock paid in, if it is paid out of the surplus profits,⁸⁴ an agreement to pay interest cannot be enforced where the corporation has no means or resources from which payment can be made, except its capital stock.⁸⁵ It would seem clear that if land in which the capital of a corporation is invested, or a part of it, is taken under the power of eminent domain, the money received as compensation therefor will

⁸¹ *De Peyster v. Insurance Co.*, 6 Paige (N. Y.) 486; *Scott v. Fire Co.*, 7 Paige (N. Y.) 198; *Lexington Life, Fire & Marine Ins. Co. v. Page*, 17 B. Mon. (Ky.) 412. Indeed, it was held in the case last cited that the safest and only allowable principle to act upon in such cases is to exclude such premiums altogether from the computation of profits.

⁸² *Main v. Milla*, 6 Biss. 98, Fed. Cas. No. 8,974.

⁸³ See *Reid v. Manufacturing Co.*, 40 Ga. 98, 104; *Wood v. Dummer*, 3 Mason, 808, Fed. Cas. No. 17,944, and 1 Cumming, Cas. Priv. Corp. 805; post, p. 563.

⁸⁴ *McLaughlin v. Railway Co.*, 8 Mich. 100.

⁸⁵ *Painesville & H. R. Co. v. King*, 17 Ohio St. 534.

take the place of the land as part of the capital, and cannot be distributed as dividends.³⁶ A sum paid in on capital stock does not become profit, and liable to distribution as profits, on the stock being forfeited for nonpayment of the balance due thereon.³⁷

In the case of a mining corporation, the profits subject to distribution are the net proceeds of its mining operations, without any deduction for decrease in value of the mine by reason of the ore being taken out. And the same principle applies to all corporations organized for the purpose of utilizing a wasting property,—a property that can be used only by consuming it,—as a mine, a lease, or a patent. Such a corporation is not to be considered as having distributed its capital merely because it has distributed the net proceeds of its operations, though the value of the property constituting its capital is necessarily thereby decreased.³⁸ Except in such cases, however, before profits can lawfully be set apart and paid out as a dividend, a proper sum must be set aside to represent the wear and tear upon the plant and property of the corporation, so that a fund will be created for the purpose of repairing and renewing the property when it shall become necessary.³⁹

Where a corporation reduces its capital stock under statutory authority, it cannot distribute among the stockholders an amount equal to the difference between the original capital stock and the reduced capital stock, without regard to the present value of its property. The reduced amount becomes the amount which it is bound to provide as capital, and which it is prohibited from depleting by payments to stockholders. It must therefore retain property actually equal in value to the amount of the reduced capital over and above its debts. If it does this, and a surplus remains, this may lawfully be distributed among the stockholders.⁴⁰

³⁶ See *Heard v. Eldredge*, 109 Mass. 258.

³⁷ *Gratz v. Redd*, 4 B. Mon. (Ky.) 178, 187.

³⁸ *Excelsior Water & Mining Co. v. Pierce*, 90 Cal. 131, 27 Pac. 44.

³⁹ *Davison v. Gillies*, 16 Ch. Div. 347, note, 2 Cumming, Cas. Priv. Corp. 223; *Dent v. Tramways Co.*, 16 Ch. Div. 344, 2 Cumming, Cas. Priv. Corp. 225.

⁴⁰ *Seeley v. Bank*, 8 Daly, 400, 78 N. Y. 608; *Strong v. Railroad Co.*, 93 N. Y. 426. "The surplus, if any, which a corporation reducing the amount of its capital, under the act of 1878, is at liberty to pay to its stockholders, must, in every case, be ascertained, and depends upon the result of an examination into its affairs, and not upon the difference between the original amount of capital and the reduced

Discretion of the Directors as to Declaring Dividend.

When a corporation has a surplus, whether a dividend shall be declared, and, if declared, how much it shall be, and when and where it shall be payable, rests largely in the discretion of the directors; and in the exercise of their discretion they will not be controlled or interfered with by the courts, unless they act fraudulently, oppressively, or unreasonably.⁴¹ The stockholders of a corporation are not entitled, as a matter of absolute right, to the payment of a dividend whenever the earnings of the corporation in any year exceed its liabilities. Though there may be a large surplus, the board of directors may, if, in their opinion, the interests of the corporation make it necessary or advisable, expend the same in improvements, or in extending the business of the corporation, if the business as extended is within its powers; or may, under some circumstances, retain it as a surplus fund, instead of dividing it among the stockholders. And whether they will do so is generally for them to decide.⁴²

Directors will not be allowed to abuse their discretion as to declaring dividends, and to use their power illegally, wantonly, or oppressively. They must act reasonably and in good faith. If the right to a dividend is clear, and there are funds from which it can properly be made, a court of equity will interfere to compel the company to declare it.⁴³

amount; and whenever, by sales of property, or by means of earnings, or otherwise, the corporation comes in possession of funds which are in excess of the reduced amount fixed as capital, it can distribute that amount without violating any law." *Strong v. Railroad Co.*, *supra*.

⁴¹ *Post*, p. 351; *Williams v. Telegraph Co.*, 93 N. Y. 162, 192, 2 Cumming, Cas. Priv. Corp. 209; *Hunter v. Roberts, Throp & Co.*, 83 Mich. 63, 47 N. W. 131; *Jackson's Adm'rs v. Plank-Road Co.*, 31 N. J. Law, 277, 2 Cumming, Cas. Priv. Corp. 201; *Belfast & M. L. R. Co. v. City of Belfast*, 77 Me. 445, 1 Atl. 362, 366; *New York, L. E. & W. R. Co. v. Nickals*, 119 U. S. 296, 7 Sup. Ct. 309, 2 Cumming, Cas. Priv. Corp. 228, W. D. Smith, Cas. Corp. 88, *Shep. Cas. Corp.* 188; *Wolfe v. Underwood*, 96 Ala. 329, 11 South. 344; *Beveridge v. Railroad Co.*, 112 N. Y. 1, 19 N. E. 489; and cases hereafter cited.

⁴² *New York, L. E. & W. R. Co. v. Nickals*, 119 U. S. 296, 7 Sup. Ct. 209, 2 Cumming, Cas. Priv. Corp. 228, W. D. Smith, Cas. Corp. 88, *Shep. Cas. Corp.* 188; *Pratt v. Pratt, Read & Co.*, 33 Conn. 446, 2 Cumming, Cas. Priv. Corp. 219; *Smith v. Manufacturing Co.*, 29 Ala. 503; *State v. Baltimore & O. R. Co.*, 6 Gill (Md.) 363.

⁴³ *Fougeray v. Cord*, 50 N. J. Eq. 185, 24 Atl. 499, 2 Cumming, Cas. Priv. Corp.

Who are Entitled to Dividends.

The profits of a corporation are to be distributed pro rata among those who are its stockholders at the time when the dividend is declared, no matter when the profits may have been earned, and without regard to the length of time particular members may have been stockholders. This is well settled.⁴⁴ And it is also well settled that the directors in declaring dividends have no right to discriminate between stockholders, unless the contract under which particular shares were issued gives them the right.⁴⁵ "The dividends must be general on all the stock, so that each stockholder will receive his proportionate share. The directors have no right to declare a dividend on any other principle. They cannot exclude any portion of the stockholders from an equal participation in the profits of the company."⁴⁶

A person who becomes a stockholder without limitations in his contract, even immediately before a dividend is declared, is entitled to share therein, and the directors cannot exclude him. In *Jones v. Terre Haute & Richmond R. Co.*⁴⁷ the plaintiff, who held bonds of the defendant corporation, by their terms convertible into stock, surrendered them, and received stock therefor. Shortly afterwards the directors declared a dividend. It was held that the plaintiff was entitled to his proportionate share, and that the board of directors could not discriminate against him.

241; *Belfast & M. L. R. Co. v. City of Belfast*, 77 Me. 445, 1 Atl. 362, 367; *Pratt v. Pratt, Read & Co.*, 33 Conn. 446, 2 Oumming, Cas. Priv. Corp. 219; *Beers v. Spring Co.*, 42 Conn. 17; *Scott v. Fire Co.*, 7 Paige (N. Y.) 198; post, p. 352.

⁴⁴ *Goodwin v. Hardy*, 57 Me. 143; *March v. Railroad Co.*, 43 N. H. 515; *Jones v. Railroad Co.*, 57 N. Y. 196; *Boardman v. Railway Co.*, 84 N. Y. 157; *Hill v. Newichawanick Co.*, 8 Hun, 459, 71 N. Y. 593; *Phelps v. Bank*, 26 Conn. 269. "This rule," says Morawetz, "is based on reasons of convenience, amounting almost to a necessity. It would be practically impossible to apportion the earnings of a corporation, whose shares are constantly changing hands, so as to give each holder a proportionate part of the profits earned while he was owner of the shares." 1 Mor. Corp. § 162.

⁴⁵ *Jones v. Railroad Co.*, 57 N. Y. 196; *Ryder v. Railroad Co.*, 13 Ill. 516; *Stoddard v. Foundry Co.*, 34 Conn. 542; *Hill v. Mining Co.* (Mo. Sup.) 21 S. W. 508.

⁴⁶ *Ryder v. Railroad Co.*, supra. Where the directors, in declaring a dividend, wrongfully except a particular stockholder, the exception is void and of no effect. *Hill v. Mining Co.*, supra.

⁴⁷ 57 N. Y. 196.

A stockholder in a corporation has no legal title to a share in the profits until a dividend is declared. Until then a transfer of his shares will carry with it the right to share in the profits already earned, and dividends subsequently declared will belong to the transferee.⁴⁸ It is otherwise with a dividend declared before the transfer, but not paid. In the absence of a special agreement to the contrary, it belongs to the transferror, and does not pass by the transfer; and the fact that the dividend is payable at a future day, or that no time for payment is fixed, can make no difference.⁴⁹ So a legatee of shares is not entitled to a dividend thereon declared before, but payable after, the death of the testator. The dividend forms part of the corpus of the estate and passes to the executor.⁵⁰ So, where the owner of stock by will directs the income of his estate to be paid to his widow, and dies after a dividend has been declared, but before it is payable, the dividend goes to the executors as part of his estate, and is not payable to the widow as income.⁵¹

Where, by the terms of a certificate of stock, the shares are transferable only on the books of the company, the corporation will be protected by a payment of dividends to the person who appears on the books as the owner of shares, if it has no notice of any transfer, and will not be liable after such payment to a person to whom the shares were transferred before the dividends were declared, but who neglected to have the transfer entered on the books.⁵² If the corpo-

⁴⁸ *Post*, p. 412; *Boardman v. Railway Co.*, 84 N. Y. 157, 177; *Jermain v. Railway Co.*, 91 N. Y. 483; *Phelps v. Bank*, 26 Conn. 269; *March v. Railroad Co.*, 43 N. H. 515; *Gemmell v. Davis*, 75 Md. 546, 23 Atl. 1032. But, if the purchaser of stock fails to comply with his contract to purchase, he loses the right, not only to the stock, but also to dividends declared after the sale. *Phinizy v. Murray*, 83 Ga. 747, 10 S. E. 358. The right to dividends not yet declared need not be separately assigned. It passes as an incident to the stock. See the cases above cited,—particularly, *Boardman v. Railway Co.*, *supra*. And see *Kaufman v. Woolen Mills Co. (Va.)* 25 S. E. 1003.

⁴⁹ *Wheeler v. Sleigh Co.*, 39 Fed. 347, 2 Cumming, Cas. Priv. Corp. 203; *Hill v. Newichawanick Co.*, 8 Hun, 459, 71 N. Y. 593; *Hopper v. Sage*, 112 N. Y. 530, 20 N. E. 350; *In re Kernochan*, 104 N. Y. 618, 11 N. E. 150; *Bright v. Lord*, 51 Ind. 272, 19 Am. Rep. 732. *Contra Burroughs v. Railroad Co.*, 67 N. C. 376, 12 Am. Rep. 611.

⁵⁰ *De Gendre v. Kent*, L. R. 4 Eq. 283; *Wheeler v. Sleigh Co.*, *supra*.

⁵¹ *In re Kernochan*, 104 N. Y. 618, 11 N. E. 150.

⁵² *Post*, p. 420; *Brisbane v. Railroad Co.*, 94 N. Y. 204, W. D. Smith, Cas.

ration has notice of the transfer, it will be liable to the transferee or his assignee for dividends subsequently declared, though the transfer is not registered, and an action may be maintained against it therefor without suing to compel it to register the transfer.⁵³ The pledgee of stock, whose name appears on the books of the corporation, or whose rights are known to the corporation, is entitled to dividends subsequently declared, as between himself and the corporation, and the corporation will be liable to him therefor if it pays them to the pledgor.⁵⁴

How Payable.

If there is no statutory or charter requirement that dividends shall be paid in cash, it is within the discretion of the directors whether they shall be made payable in cash, or in property, or whether they shall declare a stock dividend when authorized to increase the capital stock.⁵⁵ If a dividend is made payable in cash, or payable generally, the corporation becomes a debtor, and must discharge the debt, as it is bound to discharge all its other debts, in lawful currency.⁵⁶

Stock Dividends.

Where a corporation has the power to increase its capital stock, and has assets from which it may legally declare a dividend, it may, if its interests so require, hold back such assets, and issue stock therefor, instead of distributing the assets among the stockholders by de-

Corp. 94, and Shep. Cas. Corp. 177; Cleveland & M. R. Co. v. Robbins, 35 Ohio St. 483.

⁵³ Robinson v. Bank, 95 N. Y. 637, 2 Cumming, Cas. Priv. Corp. 157; Hill v. Mining Co. (Mo. Sup.) 21 S. W. 508; Gemmell v. Davis, 75 Md. 546, 23 Atl. 1032; Central Nebraska Nat. Bank v. Wilder, 82 Neb. 454, 49 N. W. 369; Guarantee Co. of North America v. East Rome Town Co., 96 Ga. 511, 23 S. E. 503; Armour v. Town Co. (Ga.) 25 S. E. 504.

⁵⁴ Boyd v. Worsted Mills, 149 Pa. St. 363, 24 Atl. 287. See, also, as to the right of a pledgee of stock to dividends: Fairbank v. Bank, 132 Ill. 120, 22 N. E. 524; Central Nebraska Nat. Bank v. Wilder, 82 Neb. 454, 49 N. W. 369; Gemmell v. Davis, 75 Md. 546, 23 Atl. 1032; Guarantee Co. of North America v. East Rome Town Co., 96 Ga. 511, 23 S. E. 503; Armour v. Town Co. (Ga.) 25 S. E. 504.

⁵⁵ Williams v. Telegraph Co., 93 N. Y. 162, 192, 2 Cumming, Cas. Priv. Corp. 209.

⁵⁶ Williams v. Telegraph Co., 93 N. Y. 162, 192, 2 Cumming, Cas. Priv. Corp. 209; Scott v. Banking Co., 52 Barb. (N. Y.) 45; Ehle v. Bank, 24 N. Y. 548.

declaring a dividend payable in money.⁵⁷ This is called a stock dividend. Such a dividend, if stock is issued only to the extent of the surplus profits, and the amount paid in as the capital stock of the corporation remains, is not a violation of the prohibition against reducing or withdrawing the capital stock by distribution among stockholders.⁵⁸

Set-Off against Debt Due to Corporation.

A corporation may retain dividends, and apply them upon debts due to it from stockholders at the time the dividend is declared.⁵⁹ This right does not rest upon any idea that the corporation has a lien, but it is the right of set-off, for the dividend is a simple debt owing by the corporation to the stockholder.⁶⁰ If shares are assigned, and notice of the assignment is given to the corporation before the dividend is declared, the right to the dividend passes to the assignee, and the corporation cannot set off a debt to it from the assignor, incurred before the assignment.⁶¹ In New York it has been held that the corporation may exercise this right of set-off if the debt became due before notice of the assignment was given, though the dividend may not have been declared until after such notice.⁶²

Remedies of Stockholders.

As has been seen, a dividend lawfully set apart from the surplus profits of a corporation becomes thereupon the individual property of the stockholders, to be received by them on demand. It is a severance from the common funds of the company of so much for the use and benefit of each stockholder in his individual right. If, upon demand by a stockholder, the corporation refuses to pay him his share, he may maintain an action against it for money had and received to his use;⁶³ or, according to some of the cases, by a suit

⁵⁷ *Williams v. Telegraph Co.*, 93 N. Y. 162, 2 Cumming, Cas. Priv. Corp. 209.

⁵⁸ *Williams v. Telegraph Co.*, *supra*.

⁵⁹ *Bates v. Insurance Co.*, 3 Johns. Cas. (N. Y.) 238; *Sargent v. Insurance Co.*, 8 Pick. (Mass.) 90; *Hagar v. Bank*, 63 Me. 509.

⁶⁰ *Gemmell v. Davis*, 75 Md. 546, 23 Atl. 1032.

⁶¹ *Gemmell v. Davis*, *supra*.

⁶² *Bates v. Insurance Co.*, *supra*.

⁶³ *King v. Railroad Co.*, 29 N. J. Law, 82, 87; *West Chester & P. R. Co. v. Jackson*, 77 Pa. St. 321, 328.

in equity.⁶⁴ If no time is fixed for payment of the dividend, but it is made payable at such time as may be directed by the board of directors, it is to be paid within a reasonable time; and if the board refuses to pay, or fix a time for payment, a stockholder may enforce his rights in equity.⁶⁵ If the directors of a corporation, in making a distribution of dividends, omit to apportion a quota thereof to certain shares of stock, the owner of such shares may maintain *assumpsit* against the corporation for breach of the contract which the law implies from the relationship of the parties, that an equal distribution of dividends will be made.⁶⁶ A demand is necessary after a dividend has been declared, before an action can be brought by a stockholder against the corporation to recover his share.⁶⁷ And it follows that interest and the statute of limitations run from the time demand is made, and only from that time.⁶⁸

The remedy of a stockholder who is wrongfully excluded from his right to share in a dividend is against the corporation.⁶⁹ He cannot follow the assets of the company into the hands of other stockholders, to whom dividends have been paid, and maintain an action against them for money had and received.⁷⁰

An action cannot be maintained against a corporation by a stockholder for a dividend, as for a debt due, until the dividend has been declared, though there may be funds from which it is the duty of the directors to declare a dividend. "A right to a dividend from the profits of a corporation is no debt until the dividend is declared. Until that time the dividend is only something that may possibly come into existence, but the obligation on the part of the corporation to declare it cannot be treated as the dividend itself."⁷¹

⁶⁴ *Le Roy v. Insurance Co.*, 2 Edw. Ch. (N. Y.) 657; *Beers v. Spring Co.*, 42 Conn. 17.

⁶⁵ *Beers v. Spring Co.*, 42 Conn. 17.

⁶⁶ *Jackson's Adm'rs v. Newark Plank-Road Co.*, 31 N. J. Law, 277, 2 Cumming, Cas. Priv. Corp. 201; *Hill v. Mining Co.* (Mo.) 21 S. W. 508.

⁶⁷ *Hagar v. Bank*, 68 Me. 509; *State v. Baltimore & O. R. Co.*, 6 Gill (Md.) 363, 387; *Bank of Louisville v. Gray*, 84 Ky. 565, 2 S. W. 168.

⁶⁸ *State v. Baltimore & O. R. Co.*, *supra*; *Bank of Louisville v. Gray*, *supra*; *Philadelphia, W. & B. R. Co. v. Cowell*, 28 Pa. St. 329.

⁶⁹ *Jones v. Railroad Co.*, 57 N. Y. 196.

⁷⁰ *Peckham v. Van Wagenen*, 83 N. Y. 40.

⁷¹ *Lockhart v. Van Alstyne*, 31 Mich. 76, per Cooley, J. And see *State v. Balti-*

If the directors unreasonably and wrongfully refuse or neglect to declare dividends when there are surplus profits out of which they may be declared, and there is no good reason for withholding them, a stockholder may maintain a suit in equity to compel them to declare and pay them.⁷² Mandamus is not a proper remedy in such a case.⁷³ Nor will mandamus lie to compel the payment of a dividend after it has been declared.⁷⁴ It must be borne in mind in this connection that it is only in a clear case that the court will interfere with the discretionary powers of the directors by compelling them to declare a dividend.⁷⁵

Remedies where Dividends are Unlawfully Paid.

If the directors or trustees act in good faith, and without negligence, they are not liable to the corporation or to creditors, at common law, for declaring and paying dividends when they should not have done so, and thereby diminishing the capital stock.⁷⁶ But if they have been guilty of a fraudulent breach of trust, or of gross negligence, in paying dividends when they had no right to pay them, they are personally liable to creditors.⁷⁷ Their liability under statutes will, of course, depend upon a construction of the statutes. Generally, they are not liable if they act in good faith, and without negligence.⁷⁸

more & O. R. Co., 6 Gill (Md.) 363; Williston v. Railroad Co., 18 Allen (Mass.) 400; Boardman v. Railway Co., 84 N. Y. 157; Hill v. Mining Co. (Mo.) 21 S. W. 508.

⁷² Fougerey v. Cord, 50 N. J. Eq. 185, 24 Atl. 499, 2 Cumming, Cas. Priv. Corp. 241; Pratt v. Pratt, Read & Co., 33 Conn. 446, 2 Cumming, Cas. Priv. Corp. 219; Beers v. Spring Co., 42 Conn. 17; Scott v. Fire Co., 7 Paige (N. Y.) 198; King v. Governor, etc., of Bank of England, 2 Barn. & Ald. 620, 2 Cumming, Cas. Priv. Corp. 218; ante, p. 347.

⁷³ Rex v. Governor, etc., of Bank of England, 2 Barn. & Ald. 620, 2 Cumming, Cas. Priv. Corp. 218.

⁷⁴ People v. Central Car & Manuf'g Co., 41 Mich. 166, 49 N. W. 925.

⁷⁵ Ante, p. 347.

⁷⁶ Excelsior Petroleum Co. v. Lacey, 63 N. Y. 422; Lexington & O. R. Co. v. Bridges, 7 B. Mon. (Ky.) 556; post, p. 515.

⁷⁷ Gratz v. Redd, 4 B. Mon. (Ky.) 178, 195; Scott v. Fire Co., 7 Paige (N. Y.) 198; post, p. 515.

⁷⁸ As to the liability under the New York statute, see Rorke v. Thomas, 56 N. Y. 559; Excelsior Petroleum Co. v. Lacey, 63 N. Y. 422; Van Dyck v. McQuade, 83 N. Y. 38; post, p. 609.

If dividends are illegally declared and paid when there are no surplus profits, they may be reclaimed either by the corporation or by its assignee for the benefit of creditors, or by the creditors themselves; and the fact that the directors acted in good faith, under a misconception as to what constituted the profits of the company out of which dividends were payable, is immaterial, for the recovery by the corporation may be sustained on the principle which allows a recovery of money paid under mistake.⁷⁹ If the capital stock of a corporation is wrongfully paid away by the directors it may be pursued by creditors into the hands of any one who is not an innocent purchaser or recipient of the same for a valuable consideration.⁸⁰ If such a wrong is threatened, a creditor may maintain a bill in equity for an injunction.⁸¹

Same—Grants and Bequests of Income and Profits.

When the owner of stock grants or bequeaths the income and profits to a person for life or for a term of years, difficult questions arise as to the right to dividends. On some points the courts do not agree, while on others the law is well settled.

A grant or bequest of the income or profits of an estate including shares of stock, does not entitle the grantee or legatee to dividends declared upon the stock before the grant or will takes effect, though they may not be payable until afterwards. Therefore, where the owner of stock left a will, by which he empowered his executors "to receive the rents, interest, and income" of so much of his estate as was given them in trust, including shares of stock, and apply the same to the use of his widow during her life, it was held that a dividend declared on the stock before his death, but not payable until afterwards, formed part of the estate, and went to the executors as such, and was not payable to the widow as income. "As soon," it was said, "as the profits in shares of stock are ascertained and declared, they cease to be the property of the company, and the owner of the shares becomes entitled to the dividend. It at once forms part of his estate. The fact that they are made payable at a future

⁷⁹ *Lexington Life, Fire & Marine Ins. Co. v. Page*, 17 B. Mon. (Ky.) 412. And see *Gratz v. Redd*, 4 B. Mon. (Ky.) 178, 189, 191; *Main v. Mills*, 6 Biss. 98, Fed. Cas. No. 8,974; *Grant v. Ross* (Ky.) 37 S. W. 263.

⁸⁰ *Gratz v. Redd*, *supra*. And see *Reid v. Manufacturing Co.*, 40 Ga. 98, 104.

⁸¹ *Reid v. Manufacturing Co.*, *supra*.

time is immaterial. The dividend to which the life tenant may be entitled as income can only be that which the company may declare after that relation is acquired. In this case the dividend represented profits or income, but had become a debt before the will took effect." ⁸²

Perhaps by the weight of authority, dividends declared after the grant or bequest takes effect, though earned before, go to the grantee or legatee as income or profits.⁸³ In some states, however, the rule is otherwise; and it is held that: "When the stock of a corporation is by the will of a decedent given in trust, the incomes thereof for the use of a beneficiary for life, with remainder over, the surplus profits which have accumulated in the lifetime of the testator, but which are not divided until after his death, belong to the corpus of his estate; while the dividends of earnings made after his death are income, and are payable to the life tenant, no matter whether the dividend be in cash or script or stock." ⁸⁴

The fact that the dividend is declared, not out of profits made by the corporation, but out of the original capital, in a case where such a dividend may be declared, is immaterial. It still goes to the legatee or grantee as income or profits from the shares.⁸⁵

⁸² In re Kernochan, 104 N. Y. 618, 11 N. E. 150. And see De Gendre v. Kent, L. R. 4 Eq. 283; Wheeler v. Sleigh Co., 39 Fed. 347, 2 Cumming, Cas. Priv. Corp. 203. But see, contra, Burroughs v. Railroad Co., 67 N. C. 376, 12 Am. Rep. 611. A bequest of "dividends," it has been held, passes a dividend declared before, but payable after, the testator's death. Cogswell v. Cogswell, 2 Edw. Ch. (N. Y.) 231.

⁸³ King v. Follett, 3 Vt. 385. And see Appeal of Merchants' Fund Ass'ns, 136 Pa. St. 43, 20 Atl. 527. But compare Smith's Appeal, infra.

⁸⁴ Smith's Appeal, 140 Pa. St. 344, 21 Atl. 438. In this case it was held that, where shares of stock are bequeathed in trust to pay the income to a certain person for life, with remainder over, profits realized from a sale by the trustees of extra shares of stock issued after testator's death, to them and other stockholders, in lieu of corporate profits applied to the improvement of the corporate property during testator's lifetime, should be distributed as capital, and not as income. And see Earp's Appeal, 28 Pa. St. 368, where there was an apportionment between a life beneficiary and the corpus of the estate of new stock representing profits earned partly before and partly after the testator's death. See, also, Cobb v. Fant, 36 S. C. 1, 14 S. E. 959.

⁸⁵ Reed v. Head, 6 Allen (Mass.) 174. In this case the cash dividends declared by a land company were held to belong to the tenant for life, though they were derived from a sale of its real estate, which was its capital. See, also, Balch v.

There is a direct conflict of opinion on the question whether, when a corporation, instead of declaring a dividend payable in cash, declares a stock dividend,—that is, a dividend payable in stock,—thereby increasing the capital stock, the new stock thus issued goes to the legatee or grantee of the income or profits, or forms part of the corpus of the estate, so as to go to the remainder-man.⁸⁶ In Massachusetts it is held that cash dividends, however large, are to be regarded as income, and go to the grantee or legatee of the income; and that stock dividends, however made, are to be regarded as an increase of the capital, and should be kept for the remainder-man. In *Minot v. Paine*,⁸⁷—a leading case,—the income of a trust fund, which included shares of stock in a corporation, was payable to a person for life, the capital then to be conveyed to another. It was held that shares of additional stock distributed to the trustee as a dividend on the original shares were to be regarded as an increase of the capital to be kept for the remainder-man, and not as income, although such shares represented net earnings of the corporation.⁸⁸ The same rule obtains in some other jurisdictions.⁸⁹ It is known as the “Massachusetts rule.” Whether the distribution by a corporation of its earnings among its stockholders is an apportionment of stock or a division of profits depends entirely upon the substance and intent of the action of the corporation, as shown by its votes. Even when, at the time of the creation of new shares to be distributed among the old stockholders, a dividend is declared in cash to the same amount, the thing received by each stockholder, whether in stock or in cash, is to be deemed capital, and not income, if such appears, upon a view of the whole action of the corporation,

Hallet, 10 Gray (Mass.) 402; *Appeal of Merchants’ Fund Ass’n*, 136 Pa. St. 48, 20 Atl. 527. So where cash dividends were declared by a manufacturing company out of money received from the sale of patent rights and a large amount of castings. *Harvard College v. Amory*, 9 Pick. (Mass.) 446.

⁸⁶ See article, 19 Am. Law Rev. 737.

⁸⁷ 99 Mass. 101, 96 Am. Dec. 705.

⁸⁸ And see *Atkins v. Albree*, 12 Allen (Mass.) 359, and cases cited below.

⁸⁹ *Gibbons v. Mahon*, 136 U. S. 549, 10 Sup. Ct. 1057, *Shep. Cas. Corp.* 194, where the question is considered at length, and the cases reviewed; *Spooner v. Phillips*, 62 Conn. 62, 24 Atl. 524; *Hotchkiss v. Quarry Co.*, 58 Conn. 120, 19 Atl. 521; *In re Brown*, 14 R. I. 371; *Greene v. Smith*, 17 R. I. 28, 19 Atl. 1081. And see *In re Kernochan*, 104 N. Y. 618, 11 N. E. 149.

to be the real character of the transaction.⁹⁰ In *Rand v. Hubbell*⁹¹ a corporation voted to increase the number of shares of its capital stock, so as to allow each stockholder to increase the number of shares held by him by one-half, and commanded the directors to do whatever was required by law for that purpose. A vote of the directors, passed on the same day, declared that a dividend in cash should be payable to each stockholder at the time within which he was allowed by the vote of the corporation to take his new shares, and should be applied by him in payment for those shares, and directed the treasurer to issue such shares to old stockholders only. Each stockholder received a check for the amount of his dividend, and immediately exchanged the check for a certificate of the shares apportioned to the stock held by him. The checks were then destroyed. It was held that the stock thus issued constituted a stock dividend, and in the case of shares of old stock held by a trustee the new shares must be considered an addition to the capital of the trust fund.

In Pennsylvania and some of the other states the Massachusetts rule is not recognized, but it is held that, where a corporation declares a dividend out of the profits payable in additional shares, such shares go to the life tenant as income.⁹² "Where a corporation," said the Pennsylvania court, "having actually made profits, proceeds to distribute such profits among the stockholders, the tenant for life would be entitled to receive them, and this without regard to the form of the transaction. Equity, which disregards form and grasps the substance, would award the thing distributed, whether stock or moneys, to whomsoever was entitled to the profits."⁹³ This has been called the "American rule";⁹⁴ but the term seems a

⁹⁰ *Daland v. Williams*, 101 Mass. 571; *Leland v. Hayden*, 102 Mass. 542; *Rand v. Hubbell*, 115 Mass. 461, 15 Am. Rep. 121.

⁹¹ 115 Mass. 461, 15 Am. Rep. 121.

⁹² *Earp's Appeal*, 28 Pa. St. 368; *Moss' Appeal*, 83 Pa. St. 264; *Appeal of Philadelphia Trust, Safe-Deposit & Ins. Co.* (Pa. Sup.) 16 Atl. 734; *Smith's Estate*, 140 Pa. St. 344, 21 Atl. 488; *Hite's Devisees v. Hite's Ex'r*, 93 Ky. 257, 20 S. W. 778. And see *Gilkey v. Paine*, 80 Me. 319, 14 Atl. 205; *In re Woodruff's Estate*, Tuck. (N. Y.) 58; *Clarkson v. Clarkson*, 18 Barb. (N. Y.) 646. But see *In re Kernochan*, 104 N. Y. 618, 11 N. E. 149.

⁹³ *Moss' Appeal*, 83 Pa. St. 264.

⁹⁴ 1 Cook, Stock, Stockh. & Corp. Law, § 554.

misnomer. The Massachusetts rule is supported by the weight of actual authority.⁹⁵

In England the rule is that an ordinary or usual dividend, whether paid in cash or in stock or property, belongs to the life tenant, while an extraordinary cash or stock or property dividend belongs to the corpus of the estate.⁹⁶

Whether, on the death of a person entitled to the income and profits of shares of stock for life, a dividend declared after his death in part out of profits earned by the corporation during his life may be apportioned between his estate and the remainder-man, is not clear. In some jurisdictions this may be done by statute, and in some it has been done independently of any statute.⁹⁷ By the weight of authority, however, in the absence of statutory provision, the whole of such a dividend goes to the remainder-man.⁹⁸ According to the well-settled rule, the estate of the life tenant is entitled to a dividend declared during his life, though not payable until afterwards.⁹⁹

INCREASE OF CAPITAL STOCK.

138. A corporation cannot, directly or indirectly, increase its capital stock beyond the amount fixed by its charter, unless the power to do so is conferred upon it by the legislature. Any attempted increase, in the absence of legislative sanction, is absolutely void.

139. Where the power to increase its capital has been conferred upon a corporation, it must be exercised by vote of the stockholders, and not by the directors.

⁹⁵ See the cases cited in notes 87-91, *supra*.

⁹⁶ 1 Cook, Stock, Stockh. & Corp. Law, §§ 556, 557, and cases there cited; *Smith's Estate*, 140 Pa. St. 344, 21 Atl. 438.

⁹⁷ *Ex parte Rutledge*, 1 Harp. Eq. (S. C.) 65, 14 Am. Dec. 696. In this case a person who was entitled for life to dividends on certain bank stock, "to be paid half-yearly as they shall be received from the bank," died just before a semiannual dividend was declared. It was held that the dividend should be apportioned, and the part which had accrued at the time of his death paid to his executor.

⁹⁸ 1 Cook, Stock, Stockh. & Corp. Law, § 558; *Foote, Appellant*, 22 Pick. (Mass.) 299.

⁹⁹ *Ante*, p. 348.

140. Where the stock of a corporation is increased, a person does not become a stockholder by merely subscribing therefor. He must pay for it.

A corporation having a fixed capital divided into a fixed number of shares has no power of its own volition, or by any act of its officers or agents, to enlarge its capital or increase the number of shares into which it is divided, unless such power is expressly conferred upon it by its charter, or by an authorized amendment thereof. The power must be conferred upon it by the legislature. Unless the power has been conferred upon it, every attempt to do so, either directly or indirectly, is void, and certificates issued in excess of the authorized capital are of no validity whatever.¹⁰⁰

Where the charter of a corporation authorizes it to increase its capital stock, the exercise of the power effects so great and radical a change in the constitution of the corporation that it must be exercised by the stockholders. It cannot be exercised by the board of directors without the consent of the stockholders, unless such authority is conferred by the charter, or in a subsequent enabling act; and such subsequent enabling act would not bind the stockholders without their acceptance of it.¹⁰¹

Where a corporation is fully organized, and increases its capital stock under power conferred by its charter, subscriptions to the new stock do not stand on the same footing as a subscription made prior to and for the purpose of effecting organization. The latter makes the subscriber a stockholder before it is paid. In the case of stock issued by a corporation after it has been organized, it is different. To constitute a subscriber for the new stock a stockholder, something more than the mere subscription is necessary. The stock must be paid for.¹⁰² The mere subscription to such stock, while it

¹⁰⁰ *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 49. In this case an officer of a corporation fraudulently issued certificates of stock in excess of the authorized capital. It was held that such certificates were void, and should be canceled at the suit of the corporation, but the corporation was held liable to persons defrauded thereby.

¹⁰¹ *Eidman v. Bowman*, 58 Ill. 444, 11 Am. Rep. 90; *Chicago City Ry. Co. v. Allerton*, 18 Wall. 233.

¹⁰² *Baltimore City Pass. Ry. Co. v. Hambleton*, 77 Md. 341, 26 Atl. 279; *St. Paul, S. & T. F. R. Co. v. Robbins*, 23 Minn. 439.

constitutes a valid contract on the part of the company to issue the stock to the subscriber upon his paying for it, and, on his part, to receive and pay for it, does not give him an interest in the company, nor vest in him the title to the stock.¹⁰³

If the stock of a corporation is increased without authority, and certificates thereof issued, the increase and the certificates are void, and can neither confer any rights, nor impose any liabilities upon the holders, except where the persons seeking to enforce the liability are bona fide creditors of the corporation, who relied upon the validity of the stock, and as against whom the holders of such stock would be estopped to deny its validity in order to escape liability.¹⁰⁴ If there was no power at all to increase the stock, creditors are chargeable with notice of the want of power, and cannot claim to have been misled, and therefore no estoppel will arise.¹⁰⁵ It is otherwise if there was power to make the increase, but a failure to comply with the preliminaries prescribed by the statute.¹⁰⁶

SAME—SHAREHOLDERS' RIGHT TO PREFERENCE.

141. The stockholders of a corporation are entitled to a preference over strangers, in proportion to their shares, in subscribing for an increase of the capital stock, and an action for damages will lie against the company if it deprives them of this right.

It is well settled that when the capital stock of a corporation is increased under a power conferred by its charter, each of the stockholders has the right to take a proportionate number of the new shares before they can be offered or issued to strangers. He may waive this right, but, if he does not, and is deprived of it, he may maintain an action against the company in assumpsit, and recover for the loss.¹⁰⁷ The measure of the damages to be recovered is the

¹⁰³ *St. Paul, S. & T. F. R. Co. v. Robbins*, *supra*.

¹⁰⁴ *Sayles v. Brown*, 40 Fed. 8; *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 49; *Veeder v. Mudgett*, 95 N. Y. 295.

¹⁰⁵ *Scovill v. Thayer*, 105 U. S. 143.

¹⁰⁶ *Veeder v. Mudgett*, 95 N. Y. 295.

¹⁰⁷ *Gray v. Bank*, 3 Mass. 364; *Eidman v. Bowman*, 58 Ill. 444, 11 Am. Rep.

excess of the market value of the stock above the par value at the time of payment of the last installment, with interest on the excess.¹⁰⁸ This rule does not apply to original stock bought in by the corporation, or taken by it for debts due to it, and which is held as assets, and sold for the payment of liabilities, or for the general benefit.¹⁰⁹

PREFERRED STOCK.

- 142.** Preference or preferred shares of stock are shares which give the holders rights and privileges which are not given to the holders of common stock,—usually the prior right to dividends to a certain amount.
- 143.** A corporation may, in the absence of prohibition in its charter, provide for the issue of preferred stock, if it does so before any stock is issued; but, by the weight of authority, it cannot do so, in the absence of legislative authority, after common stock has been issued, without the consent of the holders of such common stock, as it would thereby interfere with their vested rights under their contracts.
- 144.** It has been held that the legislature may authorize a corporation to create preferred stock by amending the charter after common stock has been issued.
- 145.** The issue of preferred stock may take the form of a borrowing; but generally the subscribers or purchasers become stockholders, and not creditors, and they have the rights and are subject to the liabilities of stockholders. Thus:
- (a) Their dividends are payable only out of the net earnings applicable to the payment of dividends, and creditors are entitled to be first paid.

⁹⁰; *Jones v. Morrison*, 31 Minn. 140, 16 N. W. 854, collecting cases; *Humboldt Driving Park Ass'n v. Stevens*, 34 Neb. 528, 52 N. W. 568; *State v. Smith*, 48 Vt. 266, 289.

¹⁰⁸ *Gray v. Bank*, *supra*.

¹⁰⁹ *State v. Smith*, 48 Vt. 266, 280.

- (b) They are subject to the statutory liability for corporate debts, if the corporation becomes insolvent.
- (c) They are entitled to vote at stockholders' meetings, and to all the other rights of stockholders, except in so far as their contract may provide otherwise.

"Preferred stock" or "preference stock" is so called because the holders are given a preference of some sort over the ordinary stockholders. The ordinary stock is called "common stock." Generally, the preference consists in the right to receive dividends from the earnings of the company before the holders of the common stock can share in such earnings.¹¹⁰ Sometimes the payment of the dividend is guarantied, in which case the stock is called "guarantied stock."¹¹¹ Preferred stock is usually issued in order to raise money for corporate purposes instead of borrowing the money on bond and mortgage, and the preference is given to facilitate its disposal.

Power to Create Preferred Stock.

Sometimes the power to issue preferred stock is expressly conferred by the charter of a corporation.¹¹² Where the charter does not expressly give the power, and does not prescribe how the shares shall be issued, but leaves the question to be determined by the corporation, and to be fixed by by-laws or otherwise, and there is no statutory prohibition in the way, a corporation may, before offering its stock, provide by its by-laws for the issuing of preferred stock, and then offer its stock to the public for subscription. Subscribers would then know what to expect, and would contract and be bound accordingly.¹¹³ By the weight of authority, however, when this is not done, but, on the contrary, the stock is divided into equal shares, and is so subscribed for, no right to create preferred stock being reserved, the stockholders acquire a vested right under their contract to share equally in the earnings of the corporation, and in its property on dissolution; and this right cannot be impaired with-

¹¹⁰ Totten v. Tison, 54 Ga. 139.

¹¹¹ Gordon's Ex'rs v. Railroad Co., 78 Va. 501.

¹¹² Belfast & M. L. R. Co. v. City of Belfast, 77 Me. 445, 1 Atl. 362.

¹¹³ See Kent v. Mining Co., 78 N. Y. 159; Davis v. Proprietors of the Second Univ. Meetinghouse, 8 Metc. (Mass.) 321.

out their consent by the subsequent creation and issue of preferred stock, unless it is done under valid legislative authority.¹¹⁴

Some of the courts hold, and some seem to hold, that a corporation has the power to create and issue preferred stock on the ground that such a transaction is virtually a borrowing of money, and that corporations have the power to borrow money, and may do it in this way.¹¹⁵ But such a transaction cannot, in any sense, be regarded as a borrowing, except, perhaps, where the preferred stock is issued as security merely, and is redeemable by the corporation.¹¹⁶ Nor

¹¹⁴ *Kent v. Mining Co.*, 78 N. Y. 159; *Campbell v. Zylonite Co.*, 122 N. Y. 455, 25 N. H. 853. And see *Banigan v. Bard*, 134 U. S. 291, 10 Sup. Ct. 565. "Shares of stock are in the nature of choses in action, and give the holder a fixed right in the division of the profits or earnings of a company so long as it exists, and of its effects when it is dissolved. That right is as inviolable as is any right in property, and can no more be taken away or lessened, against the will of the owner, than can any other right, unless power is reserved in the first instance, when it enters into the constitution of the right, or is properly derived afterwards from a superior lawgiver. The certificate of stock is the muniment of the shareholder's title, and evidence of his right. It expresses the contract between the corporation and its co-stockholders and himself; and that contract cannot, he being unwilling, be taken away from him, or changed as to him, without his prior dereliction, or under the conditions above stated." *Kent v. Mining Co.*, *supra*. Such a transaction, not being within the corporate powers of the company, is not binding upon one who holds stock under an unregistered assignment in blank as security for a debt, though consented to by the registered owner. *Campbell v. Zylonite Co.*, *supra*.

¹¹⁵ See *Hazlehurst v. Railroad Co.*, 43 Ga. 13. It was so held in *West Chester & P. R. Co. v. Jackson*, 77 Pa. St. 321, where it was said: "A corporation may issue new shares, and give them a preference, as a mode of borrowing money, where it has the power to borrow on bond and mortgage, as preferred stock is only a form of mortgage." In this case, however, provision was made for redemption of the stock, and attention was particularly called to this feature of the case by the court.

¹¹⁶ "The idea of a borrowing is not filled out unless there is in the agreement therefor a promise or understanding that what is borrowed will be repaid or returned,—the thing itself, or something like it, of equal value,—with or without compensation for the use of it in the meantime. * * * The transaction is not to be looked upon as other than a preference of one class of stockholders to another,—as giving to the first class a perpetual, inextinguishable, prior right to a portion of the earnings of the company before the other class might have anything therefrom." *Kent v. Mining Co.*, 78 N. Y. 159. The issue of preferred stock may take the form of a borrowing, as where the stock is made redeemable, and is issued, like a bond, merely as security. See *Totten v. Tison*, 54 Ga. 139; *post*, p. 367, notes 132-134.

can such a transaction be sustained under the power to make or alter by-laws, for "the power to make by-laws is to make such as are not inconsistent with the constitution and the law, and the power to alter has the same limit, so that no alteration could be made which would infringe a right already given and secured by the contract of the corporation."¹¹⁷

In several cases it has been held that an act of the legislature authorizing a corporation to issue preferred stock is valid, and not unconstitutional as impairing the obligation of the contracts between the corporation and existing stockholders, the issuing of preferred stock being regarded as a legitimate mode of raising money.¹¹⁸

Same—Laches and Estoppel of Stockholders.

Stockholders who do not consent to the creation of preferred stock must not be guilty of laches in raising objection. If the corporation, by vote of a majority of the stockholders, determines to issue preferred shares, and puts the shares on the market, or offers them on subscription, shareholders who do not consent must assert their rights without delay, so as to prevent injury to innocent third persons who may take the shares from the corporation or by transfer from subscribers. If, with knowledge of the action of the corporation, actual or constructive, they acquiesce for an unreasonable time, they will be held to have assented, and will not be heard to complain.¹¹⁹

A person who takes preferred stock in a corporation may be estopped to deny the validity of its issue as against creditors. In *Banigan v. Bard*,¹²⁰ for instance, it was held that the holder of preferred stock in a corporation issued without statutory authority, who was active in passing the resolution authorizing its issue, and who voluntarily subscribed and paid for it, and held it for 28 months, voting upon it, and using it to obtain control of the corporation's affairs, could not, upon the insolvency of the corporation, assert its invalidity, and recover the money paid for it. So it has been held

¹¹⁷ *Kent v. Mining Co.*, 78 N. Y. 159; post, p. 454.

¹¹⁸ *Rutland & B. R. Co. v. Thrall*, 35 Vt. 536, 545; *City of Covington v. Covington & Cincinnati Bridge Co.*, 10 Bush (Ky.) 69.

¹¹⁹ *Kent v. Mining Co.*, 78 N. Y. 159, where relief was held to be barred by a delay of four years.

¹²⁰ 134 U. S. 291, 10 Sup. Ct. 565, affirming 39 Fed. 13.

that persons who receive preferred stock, and for several years accept the interest guarantied to be paid thereon, cannot raise the objection that the corporation had no power to issue the stock.¹²¹

Rights and Liabilities of Preferred Stockholders.

The rights of holders of preferred stock will depend upon the construction of their contract with the corporation.¹²² Generally, they are given the right to have dividends on their stock paid out of the earnings of the corporation before anything is paid to the holders of common stock. Sometimes they are given the right to certain dividends before payment of dividends on common stock, and, in addition to this, they are entitled to share in the remaining profits pro rata with the holders of the common stock.

Ordinarily, a preferred stockholder is not to be regarded as a creditor of the corporation. He is a stockholder like the holders of common stock, the only difference being that he is entitled to a preference over them.¹²³ And it is well established that dividends on preferred stock are payable only out of the net earnings, which are applicable to the payment of dividends. They are not payable absolutely and unconditionally, but only out of profits made by the company. The preference is limited to profits whenever earned.¹²⁴

¹²¹ Branch v. Jesup, 106 U. S. 468, 1 Sup. Ct. 495, 506. Contra, American Tube Works v. Boston Mach. Co., 139 Mass. 5, 29 N. E. 63.

¹²² Of course, the charter and by-laws of the corporation in force at the time preferred stock is issued form a part of the contract between the corporation and holders of the preferred stock. See Belfast & M. L. R. Co. v. City of Belfast, 77 Me. 445, 1 Atl. 362.

¹²³ Miller v. Ratterman, 47 Ohio St. 141, 24 N. E. 496; Belfast & M. L. R. Co. v. Belfast, 77 Me. 445, 1 Atl. 362; Taft v. Railroad Co., 8 R. I. 310; Williston v. Railroad Co., 13 Allen (Mass.) 400.

¹²⁴ Lockhart v. Van Alstyne, 31 Mich. 76; Chaffee v. Railroad Co., 55 Vt. 110, W. D. Smith, Cas. Corp. 96; Miller v. Ratterman, 47 Ohio St. 141, 24 N. E. 496; Taft v. Railroad Co., 8 R. I. 310; St. John v. Railway Co., Fed. Cas. No. 12,226, affirmed 22 Wall. 136; Williston v. Railroad Co., 13 Allen (Mass.) 400. Compare Gordon's Ex'rs v. Railroad Co., 78 Va. 501. "An agreement to pay dividends on preferred stock out of the net earnings does not mean the net earnings of the corporation as it was when the preferred stock was issued. The corporation may, after the agreement, incur new obligations, which will diminish the net earnings applicable to such dividends." St. John v. Railway Co., 22 Wall. 136, affirming Fed. Cas. No. 12,226; Warren v. King, 108 U. S. 389, 2 Sup. Ct. 789, affirming 2

"A dividend among preference stockholders exclusively is understood to imply that the sum divided has been realized as profits, though the earnings do not yield a dividend to the stockholders in general."¹²⁵ Even a general guaranty of dividends on preferred stock is not a guaranty of payment in any event, but only in the event that dividends are earned.¹²⁶

If the contract with preferred stockholders merely provides that the preferred shares shall be entitled to a dividend of a certain per cent. annually when earned, the dividends are cumulative, and the arrearages of one year are payable out of the earnings of subsequent years.¹²⁷ But the dividends may be made dependent upon the profits of each particular year, and in such a case they would not be cumulative.¹²⁸

If the payment of dividends on preferred stock is made dependent upon the profits of each particular year, "as declared by the board of directors," the holders of such stock are not entitled of right to dividends payable out of the net profits accruing in any particular year, unless the directors formally declare, or ought to declare, a dividend payable out of such profits; and whether a dividend should be declared in any year is a matter belonging, in the first instance, to the directors to determine with reference to the condition of the company's property and affairs as a whole. The circumstances may jus-

Fed. 36. In *Dent v. Tramways Co.*, 16 Ch. Div. 344, 2 Cumming, Cas. Priv. Corp. 225, a corporation had unlawfully paid dividends for several years without setting apart a fund to provide for repairs and renewals by reason of wear and tear. Afterwards they sought to make up this fund out of the profits of the current year, instead of paying dividends on preferred stock, which was entitled to dividends out of the profits of the particular year only. It was held that this could not be done.

¹²⁵ Per Cooley, J., in *Lockhart v. Van Alstyne*, 31 Mich. 76.

¹²⁶ *Miller v. Ratterman*, 47 Ohio St. 141, 24 N. E. 496; *Lockhart v. Van Alstyne*, 31 Mich. 76; *Taft v. Railroad Co.*, 8 R. I. 310, and cases there cited; *Williston v. Railroad Co.*, 13 Allen (Mass.) 400.

¹²⁷ *Henry v. Railway Co.*, 3 Jur. (N. S.) 1133; *Boardman v. Railway Co.*, 84 N. Y. 157; *Hazeltine v. Railroad Co.*, 79 Me. 411, 10 Atl. 328; *Jermain v. Railway Co.*, 91 N. Y. 483. And see *Lockhart v. Van Alstyne*, 31 Mich. 76; *Cotting v. Railroad Co.*, 54 Conn. 156, 5 Atl. 851.

¹²⁸ *New York, L. E. & W. R. Co. v. Nickals*, 119 U. S. 296, 7 Sup. Ct. 209, 2 Cumming, Cas. Priv. Corp. 228, *W. D. Smith, Cas. Corp.* 88, *Shep. Cas. Corp.* 188.

tify them in expending money on improvements instead of declaring a dividend.¹²⁹

Being stockholders, the owners of preferred shares are subject to all the liabilities of stockholders, including the statutory liability for corporate debts.¹³⁰

The ownership of preferred stock, as a general rule, carries with it the right to vote upon the same at any meeting of the holders of the capital stock. But to this rule there may be exceptions. It is competent for a corporation in issuing certificates of preferred stock to stipulate therein that the holders shall not be entitled to vote the same at stockholders' meetings, and the stipulation will be binding upon them.¹³¹

Preferred stock may be issued in such a way, and under such terms, as to make the transaction strictly a borrowing; and the holders of the stock may therefore become creditors of the corporation, and not stockholders.¹³² In such a case the dividends might be payable, like the claims of other creditors, out of the gross earnings,¹³³ and the holders of the stock would not be subject to the statutory liability for debts of the corporation. "The relation of the holder of preferred stock is, in some of its aspects, similar to that of a creditor; but he is not a creditor, save as to dividends, after the same are declared. Nor does he sustain a dual relation to the corporation. He is either a stockholder or a creditor. He cannot, by

¹²⁹ *New York, L. E. & W. R. Co. v. Nickals*, supra, reversing 15 Fed. 575.

¹³⁰ *Railroad Co. v. Smith*, 48 Ohio St. 219, 31 N. E. 743.

¹³¹ *Miller v. Ratterman*, 47 Ohio St. 141, 24 N. E. 496.

¹³² In *Totten v. Tison*, 54 Ga. 139, preferred stock secured by first mortgage bonds was issued in order to procure money, under an agreement that the stock might be redeemed by the corporation, or converted into common stock, at the end of two years, at the option of the holders. At the end of the two years, the corporation being unable to redeem the shares, the certificates were surrendered by the holders, and exchanged for the mortgage bonds. The holders of the certificates never took any part or voted at stockholders' meetings, nor were they entered on the books of the corporation as stockholders. In a contest between creditors over the assets of the corporation, after insolvency, it was held that the holders of these bonds were entitled to claim as creditors. The court recognized the general rule that preferred stockholders are not in the position of creditors, but held that it did not apply to the peculiar facts of this case; that the transaction was, in effect, a loan.

¹³³ See *Gordon's Ex'rs v. Railroad Co.*, 78 Va. 501.

virtue of the same certificate, be both. If the former, he takes a risk in the concerns of the company, not only as to dividends and a proportion of assets on the dissolution of the company, but as to the statutory liability for debts in case the corporation becomes insolvent. If the latter, he takes no interest in the company's affairs, is not concerned in its property or profits as such, but his whole right is to receive agreed compensation for the use of the money he furnishes, and the return of the principal when due. Whether he is the one or the other depends upon a proper construction of the contract he holds with the company." ¹²⁴

WATERED AND BONUS STOCK.

146. By the weight of authority, in the absence of constitutional or statutory prohibition, where a corporation issues stock gratuitously, or under an agreement by which the holder is to pay less than its par value, either in money or in property or services—

- (a) The transaction is binding upon the corporation.
- (b) It is binding as against stockholders who participate or acquiesce therein.
- (c) But it is a fraud upon dissenting stockholders, and they may sue in equity to enjoin or cancel the issue.
- (d) If the stock is original stock, issued on subscription, the transaction is a fraud upon creditors of the corporation, who deal with it on the faith of the stock being full paid; and, if the corporation becomes insolvent, the original holders of such stock, and purchasers with notice, may be held liable for its par value to pay such creditors.
- (e) When a corporation is an active and going concern, it may issue stock at its market, instead of its par, value, in payment of a debt, or to raise money or purchase property necessary for carrying on its

¹²⁴ Miller v. Ratterman, 47 Ohio St. 141, 24 N. E. 496.

business, and, if the stock is issued as full paid, and the transaction is in good faith, the holders of the stock will not be liable to creditors.

(f) If stock is issued as a bonus, and without consideration, the holders will be liable for the par value of the stock to creditors who deal with the corporation on the faith of the stock being full paid. This rule is not recognized in New York.

(g) In any case, only those creditors who have dealt with the corporation on the faith of the stock being full paid can complain. Therefore, the holders of stock issued as full paid, without being paid in fact, are not liable

(1) To persons who became creditors before the stock was issued.

(2) Or who became creditors with knowledge of the facts.

147. In the absence of constitutional or statutory prohibition, stock may be paid for in property or services, if they are such as the corporation has the power to purchase or engage; and by the weight of authority the transaction will be valid as against creditors, if it was free from fraud, though the property may in fact have been worth less than the stock. If the overvaluation is intentional, the transaction is fraudulent as a matter of law, and obvious and gross overvaluation, if unexplained, is conclusive evidence of intentional overvaluation.

148. These rules are to some extent inapplicable under peculiar constitutional or statutory provisions in force in some states.

Effect as to the Corporation.

In the absence of constitutional or statutory prohibition, or express prohibition in its charter, a corporation may bind itself by an issue of stock as full paid on receipt of partial payment only, either

virtue of the same certificate, be both. If the former, he takes a risk in the concerns of the company, not only as to dividends and a proportion of assets on the dissolution of the company, but as to the statutory liability for debts in case the corporation becomes insolvent. If the latter, he takes no interest in the company's affairs, is not concerned in its property or profits as such, but his whole right is to receive agreed compensation for the use of the money he furnishes, and the return of the principal when due. Whether he is the one or the other depends upon a proper construction of the contract he holds with the company."¹⁸⁴

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Effect as to the Corporation.

In the absence of constitutional or statutory prohibition, or express prohibition in its charter, a corporation may bind itself by an issue of stock as full paid on receipt of partial payment only, either

virtue of the same certificate, be both. If the former, he takes a risk in the concerns of the company, not only as to dividends and a proportion of assets on the dissolution of the company, but as to the statutory liability for debts in case the corporation becomes insolvent. If the latter, he takes no interest in the company's affairs, is not concerned in its property or profits as such, but his whole right is to receive agreed compensation for the use of the money he furnishes, and the return of the principal when due. Whether he is the one or the other depends upon a proper construction of the contract he holds with the company." ¹⁸⁴

WATERED AND BONUS STOCK

146. By the weight of authority, in the absence of constitutional or statutory prohibition, where a corporation issues stock gratuitously, or under an agreement by which the holder is to pay less than its par value, either in money or in property or services—

- (a) The transaction is binding upon the corporation.
- (b) It is binding as against stockholders who participate or acquiesce therein.
- (c) But it is a fraud upon dissenting stockholders, and they may sue in equity to enjoin or cancel the issue.
- (d) If the stock is original stock, issued on subscription, the transaction is a fraud upon creditors of the corporation, who deal with it on the faith of the stock being full paid; and, if the corporation becomes insolvent, the original holders of such stock, and purchasers with notice, may be held liable for its par value to pay such creditors.
- (e) When a corporation is an active and going concern, it may issue stock at its market, instead of its par, value, in payment of a debt, or to raise money or purchase property necessary for carrying on its

¹⁸⁴ *Miller v. Ratterman*, 47 Ohio St. 141, 24 N. E. 496.

business, and, if the stock is issued as full paid, and the transaction is in good faith, the holders of the stock will not be liable to creditors.

(f) If stock is issued as a bonus, and without consideration, the holders will be liable for the par value of the stock to creditors who deal with the corporation on the faith of the stock being full paid. This rule is not recognized in New York.

(g) In any case, only those creditors who have dealt with the corporation on the faith of the stock being full paid can complain. Therefore, the holders of stock issued as full paid, without being paid in fact, are not liable

(1) To persons who became creditors before the stock was issued.

(2) Or who became creditors with knowledge of the facts.

147. In the absence of constitutional or statutory prohibition, stock may be paid for in property or services, if they are such as the corporation has the power to purchase or engage; and by the weight of authority the transaction will be valid as against creditors, if it was free from fraud, though the property may in fact have been worth less than the stock. If the overvaluation is intentional, the transaction is fraudulent as a matter of law, and obvious and gross overvaluation, if unexplained, is conclusive evidence of intentional overvaluation.

148. These rules are to some extent inapplicable under peculiar constitutional or statutory provisions in force in some states.

Effect as to the Corporation.

In the absence of constitutional or statutory prohibition, or express prohibition in its charter, a corporation may bind itself by an issue of stock as full paid on receipt of partial payment only, either

itors by subscriptions to the stock of a corporation cannot be defeated by a simulated payment of such, nor by any device short of actual payment in good faith; and, while any settlement or satisfaction of such subscription may be good as between the corporation and the stockholders, it is unavailing as against the claims of creditors." ¹⁴⁹ The supreme court of Minnesota in a late case holds, in an opinion by Judge Mitchell, that the rule is not based on any trust-fund doctrine at all, but upon the ground of fraud,—the fraud consisting in impliedly representing to the public that the stock has been paid in full, when it has been paid in part only, or when nothing at all has been paid. "By putting it upon the ground of fraud," it was said, "and applying the old and familiar rules of law on that subject to the peculiar nature of a corporation and the relation which its stockholders bear to it and to the public, we have at once rational and logical ground on which to stand. The capital of a corporation is the basis of its credit. It is a substitute for the individual liability of those who own its stock. People deal with it and give it credit on the faith of it. They have a right to assume that it has paid-in capital to the amount which it represents itself as having; and if they give it credit on the faith of that representation, and if the representation is false, it is a fraud upon them; and, in case the corporation becomes insolvent, the law, upon the plainest principles of common justice, says to the delinquent stockholder, 'Make that representation good by paying for your stock.' It certainly cannot require the invention of any new doctrine in order to enforce so familiar a rule of equity. It is the misrepresentation of fact in stating the amount of capital to be greater than it really is that is the true basis of the liability of the stockholder in such cases." ¹⁵⁰

Same—Increase of Capital Stock.

Where the capital stock of a corporation is increased, if the increase is for the purpose of adding to the original capital stock, and enabling the corporation to do a larger and more profitable business,

¹⁴⁹ *Camden v. Stuart*, 144 U. S. 104, 12 Sup. Ct. 585.

¹⁵⁰ *Hospes v. Car Co.*, 48 Minn. 174, 50 N. W. 1117, 1 Cumming, Cas. Priv. Corp. 885. See post, p. 539, where the trust-fund doctrine is discussed.

subscribers to or purchasers of such stock stand practically upon the same basis as subscribers to the original stock; and they are liable for the par value of the stock.¹⁵¹ In *Flinn v. Bagley*¹⁵² the defendants had subscribed and agreed to pay certain sums of money towards the increased capital stock of a corporation, with the understanding that they were to receive stock therefor at 66⅔ cents on the dollar, which was all the existing stock was worth, and all that the new stock could be sold for. The arrangement having been carried out, and certificates of stock issued, it was held that, though the case was a hard one upon the defendants, and no fraud was intended, the assignee in bankruptcy of the corporation could hold them for the remaining one-third of the par value of the stock. If a corporation increases its capital stock, and distributes part of the new stock among the stockholders as full paid, without any consideration, they will be liable to creditors of the corporation for its par value.¹⁵³

Same—Issue of Stock at Market Value by Active Corporation to Pay Debts, etc.

As has just been shown, in the case of original subscriptions to the capital stock of a corporation, and subscriptions to an increase of stock, the par value must be paid to protect the subscriber against the claims of creditors. A distinction has been made between these cases and cases in which an active corporation issues stock for the purpose of paying its debts, or for the purpose of procuring money for the prosecution of its business where its original capital has become impaired by loss or misfortune; and it has been held that in the latter cases, in the absence of constitutional or statutory prohibition, it may issue stock as full paid on payment of its actual value, instead of its par value; and, if the transaction is honest and fair, the holders of the stock will not be liable to creditors on the theory that the stock is not paid up. There are some decisions

¹⁵¹ *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855; *Flinn v. Bagley*, 7 Fed. 785, 1 Cumming, Cas. Priv. Corp. 845; *Rickerson Roller-Mill Co. v. Farrell Foundry & Mach. Co.*, 75 Fed. 554.

¹⁵² 7 Fed. 785, 1 Cumming, Cas. Priv. Corp. 845.

¹⁵³ *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855.

against this view,¹⁵⁴ but it is supported by reason and by the weight of authority.¹⁵⁵

In *Clark v. Bever*,¹⁵⁶ decided in 1891, a railroad company, of which the defendant's intestate was president and a stockholder, had a settlement with a construction company, of which he was also a member, for work done in building the road. The railroad company, being unable to pay the claim of the construction company, delivered to it 3,500 shares of its stock at 20 cents on the dollar, and they were accepted in full satisfaction of the debt. The stock was not worth anything on the market, and was issued directly to the defendant's intestate, and no other payment than the 20 per cent. was ever made on the stock. A judgment creditor of the railroad company filed a bill to compel the payment by the defendant of his claim upon the theory that he was liable for the par value of the stock, whatever may have been its market value at the time it was issued. It was held that he could not recover.

So also, by the weight of authority, in the absence of constitutional or statutory prohibition, where an active corporation finds its original capital impaired by loss or misfortune, it may, for the purpose of recuperating itself and providing new conditions for the successful prosecution of its business, issue new stock, when authorized to increase its capital stock, and may put it upon the market and sell it for the best price that can be obtained; and if the sale is fairly made, the purchasers cannot be held liable to creditors of the corporation, on its becoming insolvent, for the difference between the amount paid by them and the par value of the stock.¹⁵⁷ In *Handley*

¹⁵⁴ *Jackson v. Traer*, 64 Iowa, 469, 20 N. W. 764, Rothrock, O. J., and Seevers, J., dissenting (disapproved in *Clark v. Bever*, *infra*).

¹⁵⁵ *Clark v. Bever*, 139 U. S. 96, 11 Sup. Ct. 468; *Fogg v. Blair*, 139 U. S. 118, 11 Sup. Ct. 476; *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855; *Van Cott v. Van Brunt*, 82 N. Y. 535; *Stein v. Howard*, 65 Cal. 616, 4 Pac. 662.

¹⁵⁶ 139 U. S. 96, 11 Sup. Ct. 468. See, also, *Fogg v. Blair*, 139 U. S. 118, 11 Sup. Ct. 476; *Union Loan & Trust Co. v. Southern California Motor-Road Co.*, 51 Fed. 840.

¹⁵⁷ As we have seen, this does not apply where the stock is increased for the purpose of providing a larger capital and doing an extended business, and not to restore capital impaired by losses. *Ante*, p. 374.

v. Stutz,¹⁵⁸ an active corporation, for the purpose of paying its debts, and obtaining money to prosecute its business, issued bonds; but, finding it impossible to negotiate them, it issued shares of capital stock in an amount equaling the par value of the bonds as an additional inducement to their purchase. The bonds and stock were sold at a price fairly representing their market value, without any unfair dealing on the part of any one connected with the transaction. Under these circumstances it was held that the purchasers could not be called upon to respond for the par value of the stock at the suit of the creditors of the corporation. "To say," said the court, "that a corporation may not, under the circumstances above indicated, put its stock upon the market, and sell it to the highest bidder, is practically to declare that a corporation can never increase its capital by a sale of shares, if the original stock has fallen below par. The wholesome doctrine, so many times enforced by this court, that the capital stock of an insolvent corporation is a trust fund for the payment of its debts, rests upon the idea that the creditors have a right to rely upon the fact that the subscribers to such stock have put into the treasury of the corporation, in some form, the amount represented by it; but it does not follow that every creditor has a right to trace each share of stock issued by such corporation, and inquire whether its holder, or the person of whom he purchased, has paid its par value for it. It frequently happens that corporations, as well as individuals, find it necessary to increase their capital in order to raise money to prosecute their business successfully, and one of the most frequent methods resorted to is that of issuing new shares of stock and putting them upon the market for the best price that can be obtained; and, so long as the transaction is bona fide, and not a mere cover for 'watering' the stock, and the consideration obtained represents the actual value of such stock, the courts have shown no disposition to disturb it. Of course, no one would take stock so issued at a greater price than the original stock could be purchased for, and hence the ability to negotiate the stock and to raise the money must depend upon the fact whether the purchaser shall or shall not be called upon to respond for its par value."¹⁵⁹

¹⁵⁸ 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855.

¹⁵⁹ See, also, *Stein v. Howard*, 65 Cal. 616, 4 Pac. 662; *Dummer v. Smedley* (Mich.) 68 N. W. 260.

If an active corporation can issue stock at its market value in payment of its debts, or to raise money necessary to carry on its business, as held in the cases referred to above, there seems to be no good reason why they cannot issue stock at its market value in payment for property or services which are necessary for the prosecution of its business, and which it can procure in no other way, and which it has the power to purchase or engage. And there are cases which hold that it can do so if the transaction is honest and fair. In *Van Cott v. Van Brunt*¹⁶⁰ a railroad company in good faith made a contract for the construction of its road, and agreed to pay therefor in its stock on the basis of its actual, instead of its par, value. The court of appeals of New York held that the contract was valid, and that the holders of the stock could not be held liable to creditors for the difference between what was thus paid and its par value. This decision has been criticized by text writers and by some of the courts, but it has often been approved, and has lately been reaffirmed by the New York court.

Same—Gratuitous Issue of Stock.

In New York it is held that the liability of a shareholder in a corporation to pay for stock does not arise out of the relation, but depends upon his contract with the corporation, express or implied, or upon some statute fixing his liability, and that, in the absence of either contract or statute, one to whom shares have been issued as a gratuity does not, by accepting them, commit any wrong upon creditors, or make himself liable to pay the par value of the shares for the payment of corporate debts.¹⁶¹ According to the better opinion, however, the rule is otherwise; and if a person accepts stock in a corporation, which is issued to him as a gratuity, and the corporation becomes insolvent, the law will create a promise to pay therefor in favor of creditors.¹⁶²

¹⁶⁰ 82 N. Y. 535. See dictum in *Barr v. Railroad Co.*, 125 N. Y. 263, 26 N. E. 145. And see *Coe v. Railroad Co.*, 52 Fed. 531.

¹⁶¹ *Christensen v. Eno*, 106 N. Y. 97, 12 N. E. 648.

¹⁶² *Stutz v. Handley*, 41 Fed. 531; *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530; 1 *Cumming, Cas. Priv. Corp.* 855. And see *Skrainka v. Allen*, 7 Mo. App. 434, 76 Mo. 384; *Washburn v. Green*, 133 U. S. 30, 10 Sup. Ct. 280; *Marrow v. Steel Co.*, 87 Tenn. 262, 10 S. W. 495.

Same—Payment for Stock in Property or Services.

It is clear on principle, and well established by authority, that the directors of a corporation, in the absence of constitutional or statutory prohibition, may receive property or services in payment for stock, either from original subscribers or from persons to whom they sell stock, in any case in which they would have the power to purchase the property or contract for the services.¹⁶³ Such power is often expressly conferred by statute, but this is not necessary, for it exists at common law. Where the directors have the power to contract a debt for property or services, it would be absurd to say that they cannot pay for the same in stock, or receive the same in payment of subscriptions, and to require them to first contract the debt, and then pay it with money received for stock or on subscriptions. Whether the stock must be paid for at its par value instead of its market value has been considered in the preceding paragraphs, and it has been seen that subscribers must pay the par value, but that, by the weight of authority, an active corporation may sometimes issue stock in payment of debts, or to raise money for the prosecution of its business, at its market value.

Same—Value of the Property or Services.

It is expressly provided by statute in some jurisdictions that property or services received in payment for stock must be taken at their money value. This is nothing more than a declaration of the common law in so far as dissenting stockholders and subsequent creditors of the corporation are concerned. Even in the absence of such a statute, for a corporation to issue stock for property intentionally overvalued would be a fraud upon dissenting stockholders; and, even if all the stockholders should consent, it would be a fraud upon persons dealing with the corporation. Dissenting stockholders could sue to enjoin the issue of stock for property intentionally overvalued, or to cancel it if issued; and persons afterwards dealing with the corporation could hold the persons to whom the stock is thus issued liable for the difference between the amount of their stock and the real value of the property.

¹⁶³ Carr v. Le Fevre, 27 Pa. St. 413; Brant v. Ehlen, 59 Md. 1; Liebke v. Knapp, 79 Mo. 22, 49 Am. Rep. 212; Coffin v. Ransdell, 110 Ind. 417, 11 N. E. 20; Spargo's Case, 8 Ch. App. 407, 412.

Where a corporation receives property or services in payment for stock, and issues the stock as full paid, actual fraud or intentional overvaluation of the property or services must be shown before the holders of the stock can be held liable to creditors of the corporation on the ground that the stock is not full paid. It is not enough to show an overvaluation due to mere error of judgment.¹⁶⁴ "The transaction may be impeached for fraud, but not for error of judgment, or mistaken views of the value of the property, inasmuch as good faith and the exercise of an honest judgment is all that is required."¹⁶⁵ In *Gamble v. Queens County Water Co.*¹⁶⁶ a shareholder in a water company, at his own expense, and for his own benefit, built a system of pipes, etc., suitable for an extension of the company's plant, and the corporation purchased the same from him, issuing in payment stocks and bonds of the value of \$110,000. The cost of the work was from \$80,000 to \$85,000. It was held that the difference was not so large as to necessarily indicate fraud, and the transaction was upheld.

Some of the cases hold that an actual fraudulent intent must be shown in order that a person who pays for his stock in property may be held liable to creditors on the ground that the property was overvalued, and some opinions contain dicta to this effect.¹⁶⁷ But by the better opinion this is not necessary. The directors of a corporation have no right to take in payment for stock property that is in-

¹⁶⁴ *Coit v. Amalgamating Co.*, 119 U. S. 343, 7 Sup. Ct. 231, 1 Cumming, Cas. Priv. Corp. 847 (as construed in *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855); *Bank of Ft. Madison v. Alden*, 129 U. S. 372, 9 Sup. Ct. 332; *Schenck v. Andrews*, 57 N. Y. 133; *Douglass v. Ireland*, 73 N. Y. 100; *Lake Superior Iron Co. v. Drexel*, 90 N. Y. 87; *Gamble v. Water Co.*, 123 N. Y. 91, 25 N. E. 201.

¹⁶⁵ *Douglass v. Ireland*, 73 N. Y. 100.

¹⁶⁶ 123 N. Y. 91, 25 N. E. 201.

¹⁶⁷ See *Phelan v. Hazard*, 5 Dill. 45, Fed. Cas. No. 11,068; *Coit v. Amalgamating Co.*, 119 U. S. 343, 7 Sup. Ct. 231, 1 Cumming, Cas. Priv. Corp. 847; *Young v. Iron Co.*, 65 Mich. 111, 31 N. W. 814; *Whitehill v. Jacobs*, 75 Wis. 474, 44 N. W. 630; *Coffin v. Ransdell*, 110 Ind. 417, 11 N. E. 20; *Clow v. Brown* (Ind. Sup.) 31 N. E. 361; *Carr v. Le Fevre*, 27 Pa. St. 413; *Brant v. Ehlen*, 59 Md. 1; *Bickley v. Schlag*, 46 N. J. Eq. 533, 20 Atl. 250; *Clayton v. Knob Co.*, 109 N. C. 385, 14 S. E. 37; *Walburn v. Chenault*, 43 Kan. 352, 23 Pac. 657; *Grant v. Railroad Co.*, 4 O. O. A. 511, 54 Fed. 569.

tentionally overvalued. Laying aside all question as to whether there is an actual intention to defraud, such a transaction would be a fraud in law, both upon dissenting stockholders and upon persons dealing with the corporation on the faith of its stock being fully paid up, and it would be just as invalid as against creditors as a payment for stock in money at a discount. If the nature of the property and the extent of the overvaluation are such that the overvaluation may possibly have been due to error of judgment, then, to render the transaction invalid as against creditors, actual fraud must be shown, and the question is one of fact.¹⁶⁸ If, on the other hand, the overvaluation is so gross and obvious that it could not have been due to mere error of judgment, the transaction will be held fraudulent as a matter of law.¹⁶⁹ This seems to be the fair result of the cases, if the opinions are read in the light of the facts actually before the court.

In *Wetherbee v. Baker*¹⁷⁰ five persons agreed for the purchase of a tract of land, and organized themselves into a corporation under a land improvement act. In the certificate of incorporation the capital stock was fixed at \$100,000, and these persons subscribed for all of it, and became the directors of the company. The consideration of the purchase was \$50,000. The deed was made directly to the corporation, and it gave its obligations for the whole purchase money. The directors then appraised the lands at \$100,000, and credited \$50,000 of the valuation as a credit of 50 per cent. on the subscriptions. The land was not worth more than the original purchase money, and the corporation acquired no other property. It was held that, as against creditors of the corporation, the allowance of a credit of 50 per cent. on the subscriptions was invalid, and that the stockholders

¹⁶⁸ See *Douglass v. Ireland*, 73 N. Y. 100; *Lake Superior Iron Co. v. Drexel*, 90 N. Y. 87.

¹⁶⁹ See *Boynton v. Andrews*, 63 N. Y. 93; *Boynton v. Hatch*, 47 N. Y. 225; *National Tube-Works Co. v. Gilfillan*, 124 N. Y. 302, 26 N. E. 538; *Wetherbee v. Baker*, 35 N. J. Eq. 501; *Shickle v. Watts*, 94 Mo. 410, 7 S. W. 274; *Northwestern Mut. Life Ins. Co. v. Cotton-Exchange Real-Estate Co.*, 46 Fed. 22; *Elyton Land Co. v. Birmingham Warehouse & Elevator Co.*, 92 Ala. 407, 9 South. 129, 1 Cumming, Cas. Priv. Corp. 870; *Boulton Carbon Co. v. Mills*, 78 Iowa, 460, 43 N. W. 291; *First Nat. Bank of Deadwood v. Gustin Minerva Con. Min. Co.*, 42 Minn. 327, 44 N. W. 198; 1 Cumming, Cas. Priv. Corp. 850; *Garrett v. Mining Co.*, 113 Mo. 330, 20 S. W. 965. Compare *Libby v. Tobey* (Me.) 19 Atl. 904.

¹⁷⁰ 35 N. J. Eq. 501.

were liable for the whole amount of their subscriptions as they appeared in the certificate of incorporation.

In *Douglass v. Ireland*¹⁷¹ the entire capital stock of a corporation, \$300,000, was issued to one of its trustees in consideration of the assignment to the company of two contracts for the purchase of mining property, upon which nothing had been paid, the contract price being \$40,000. One-third of the stock was immediately transferred to the company, to be sold to raise a working capital, and was sold at from 40 to 60 cents on the dollar. Defendant, knowing the circumstances, and having participated as trustee of the corporation in the transaction, purchased \$25,000 of the stock at 40 cents. The jury found the value of the property to be \$68,000. It was held that the evidence justified a finding of fraud, and that the defendant was liable to creditors of the corporation.

When property taken by a corporation in payment for stock is not only grossly overvalued, but there are other circumstances from which actual fraudulent intent may be inferred, there can be no question but that the stockholder is liable to subsequent creditors of the corporation, who became such in ignorance of the circumstances under which the stock was issued, for the difference between the value of the property and the par value of the stock.¹⁷²

In determining the value of property thus received in payment for stock, the true valuation is the value to the company; and where the property has been produced by the labor and at the expense of the person from whom it is received, a fair profit to him is to be included.¹⁷³ If the property is taken by the corporation at an honest val-

¹⁷¹ 73 N. Y. 100.

¹⁷² *Lloyd v. Preston*, 146 U. S. 630, 13 Sup. Ct. 131, affirming 36 Fed. 54.

¹⁷³ *Gamble v. Water Co.*, 123 N. Y. 91, 25 N. E. 201. In this case a shareholder in a water company, having built a system of pipes, etc., suitable for an extension of the company's plant, and having sold the same to the corporation for stock and bonds, it was held that, in determining the value of the property, the question was the value to the company, and that there should be included in the estimate, in addition to the money actually expended for labor and materials, an adequate charge by the owner and his assistant for personal services in superintending the work, interest upon the money invested, amounts saved by fortunate purchases of material, and a reasonable profit upon the undertaking, having regard to the nature and risks of the work. As to the elements to be considered in estimating value, see *Camden v. Stuart*, 144 U. S. 104, 12 Sup. Ct. 585.

nation, fairly made and agreed upon, the transaction will not be rendered invalid by the fact that its value, estimated in the light of subsequent events, does not equal the amount at which it was received.¹⁷⁴ It will be presumed, in the absence of any proof as to the value of property received in payment for stock, that it was adequate.¹⁷⁵

Same—Creditors Who Cannot Complain.

The true reason why creditors of an insolvent corporation can hold the persons to whom the corporation has issued stock as full paid, when nothing at all, or only a part of it, has been paid, being that holding such stock out to the public as full paid is a fraud upon persons dealing with the corporation on the faith of the stock being actually fully paid for, only those creditors who come within the reason of the rule can complain.¹⁷⁶ It follows that creditors cannot attack a transaction by which a corporation has issued stock gratuitously or for a cash discount, or for property worth less than the amount of the stock, if they knew the facts, and did not give credit to the corporation in the belief that the stock was fully paid. In *Coit v. North Carolina Gold Amalgamating Co.*¹⁷⁷ it was held that where, upon the purchase of additional property by a corporation, its capital stock was increased by the issue to the stockholders, upon the surrender of their old certificates, of new stock to a much greater extent than the value of the additional property, the stockholders could not be held liable on the stock at the suit of a creditor who was cognizant of the whole transaction, and acquiesced in it.¹⁷⁸ So, when the stock of a corporation is increased, and the increased stock issued for less than its value, persons who became creditors of the corporation prior to the increase cannot hold the purchasers or holders of

¹⁷⁴ *Coit v. Amalgamating Co.*, 119 U. S. 343, 7 Sup. Ct. 231, 1 Cumming, Cas. Priv. Corp. 847; *Carr v. Le Fevre*, 27 Pa. St. 413.

¹⁷⁵ *Davis v. Chemical Co.*, 101 Ala. 127, 8 South. 496.

¹⁷⁶ *Ante*, p. 374.

¹⁷⁷ 119 U. S. 343, 7 Sup. Ct. 231, 1 Cumming, Cas. Priv. Corp. 847.

¹⁷⁸ And see *Whitehill v. Jacobs*, 75 Wis. 474, 44 N. W. 630; *First Nat. Bank v. Gustin Minerva Con. Min. Co.*, 42 Minn. 327, 44 N. W. 198, 1 Cumming, Cas. Priv. Corp. 850; *Hospes v. Car Co.*, 48 Minn. 174, 50 N. W. 1117, 1 Cumming, Cas. Priv. Corp. 885; *Rickerson Roller-Mill Co. v. Farrell Foundry & Machine Co.*, 75 Fed. 554.

such stock liable for its value; for they could not, by any legal presumption, have trusted the corporation upon the faith of such stock.¹⁷⁹ But persons who become creditors after the increase is voted are entitled to look to those who subsequently receive the stock, though their debts are contracted before the stock is received.¹⁸⁰

"The whole doctrine that the capital stock of corporations is a trust fund for the payment of creditors rests upon the equitable consideration that the distribution of the capital among stockholders without making adequate provision for the payment of debts, or the issue of fictitiously paid-up stock, is a fraud upon creditors who contract with the corporation in reliance upon its capital remaining intact, or in reliance upon the professed capital having been in fact paid up in full. But, when the reason for the rule does not exist, the rule itself ceases to apply. This trust does not arise absolutely in every case in favor of any and every creditor. It is not true, and no case can be found which holds, that it is in the power of a creditor in every and all cases, as a matter of right, to institute an inquiry as to the value or amount of the consideration given for stock issued as fully paid up, any more than it would be his right, in any and every case, to inquire into the distribution of the capital among the shareholders. It is only those creditors who can fairly allege that they have relied, or whom the law presumes to have relied, upon the amount of capital stock of the company, who have a right to make such inquiry, or in whose favor equity will impress a trust upon the subscription to the stock, and set aside a fictitious arrangement for its payment."¹⁸¹

Effect of Constitutional and Statutory Provisions.

In a number of states constitutional or statutory provisions have been adopted or enacted with a view to preventing the issue of watered stock. These provisions vary somewhat in the different states.

¹⁷⁹ *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855, affirming 41 Fed. 531. And see *Graham v. Railroad Co.*, 102 U. S. 148, 1 Cumming, Cas. Priv. Corp. 1006.

¹⁸⁰ *Handley v. Stutz*, *supra*.

¹⁸¹ *First Nat. Bank v. Gustin Minerva Con. Min. Co.*, 42 Minn. 327, 44 N. W. 198, 1 Cumming, Cas. Priv. Corp. 850.

Even where they are similar, the courts have not always agreed in construing them.

In quite a number of states it is provided, in substance, that no corporation shall issue stock except for labor done, services performed, or money or property actually received; and all fictitious increase of stock shall be void. If effect is given to the language of this statute, it seems clear that stock issued by a corporation without any consideration at all is absolutely void, and the holders do not become stockholders at all for any purpose. It was so held by the supreme court of Colorado, where a holder of such stock sought to maintain an action, the right to maintain which depended upon his being a stockholder.¹⁸² It would seem to follow necessarily from this construction that the corporation could refuse to recognize him as a stockholder, and that he could not be held liable to creditors.¹⁸³ A contract which contemplates the violation of this provision is illegal and void.¹⁸⁴ While a contract by a corporation to issue stock in violation of the statute for labor and property is executory, the corporation may maintain a suit to rescind the contract.¹⁸⁵ In such a case it has been held the contractor may recover from the corporation the value of the labor and materials actually furnished by him, if his conduct has been free from actual bad faith.¹⁸⁶ By the better opinion, a person who has entered into a contract to take stock to be issued in violation of the statute may withdraw before it is issued, and recover money paid by him under the contract, for, if an illegal agreement is not *malum in se*, but merely *malum prohibitum*, a *locus poenitentiae* remains; and, while the illegal object has not been carried out by performance of the agreement, it may be repudiated, and money paid under it may be recovered.¹⁸⁷ But, if the stock has been issued, and the illegal ob-

¹⁸² *Arkansas River L. T. & C. Co. v. Farmers' Loan & Trust Co.*, 18 Colo. 587, 22 Pac. 954.

¹⁸³ But see *Nenny v. Waddill*, 6 Tex. Civ. App. 244, 25 S. W. 308.

¹⁸⁴ *Williams v. Evans*, 87 Ala. 725, 6 South. 702; *Garrett v. Mining Co.*, 113 Mo. 830, 20 S. W. 965.

¹⁸⁵ *New Castle Northern Ry. Co. v. Simpson*, 21 Fed. 533.

¹⁸⁶ *New Castle Northern Ry. Co. v. Simpson*, *supra*.

¹⁸⁷ *Congress & Empire Spring Co. v. Knowlton*, 103 U. S. 49, affirming 14 Blatchf. 364, Fed. Cas. No. 7,903; *Clark*, Cont. 494. Contra, *Knowlton v. Spring Co.*, 57 N. Y. 518.

ject thereby carried out, such an action cannot be maintained.¹⁸⁸

The constitution of Arkansas provides that "no private corporation shall issue stocks or bonds except for money or property actually received or labor done, and all fictitious increase of stock or indebtedness shall be void." In *Memphis & L. R. R. Co. v. Dow*¹⁸⁹ the supreme court of the United States, construing this provision, held that it was not intended to make the validity of every issue of stock or bonds by a private corporation depend upon the inquiry whether the money, property, or labor actually received therefor was of equal value in the market with the stock or bonds so issued; or to restrict corporations, acting with the approval of their stockholders, in the exchange of their stock or bonds for money, property, or labor, upon such terms as they may deem proper, provided the transaction is a real one, based upon a present consideration, and having reference to legitimate corporate purposes, and is not a mere device to evade the law. And the court held that the provision did not prevent mortgage bondholders, who bought in the property and franchises of a corporation upon foreclosure, from fixing the terms upon which they would surrender those interests, and that they might reorganize upon substantially the same basis, as to capital stock and bonded indebtedness, as that of the old corporation, although under that arrangement they received both stock and bonds to a large amount, of which the amount of the stock alone was sufficient to cover the full value of the property, rights, and privileges of the reorganized company.

In California, under such a provision, it was held that an increase of stock in a water company, and an issue of the same at the actual market value, which was less than the par value, for the purpose of enlarging the works, was not a fictitious issue, and was authorized.¹⁹⁰

In *Peoria & S. R. Co. v. Thompson*¹⁹¹ it was held that a similar

¹⁸⁸ *Clarke v. Lumber Co.*, 59 Wis. 655, 18 N. W. 492.

¹⁸⁹ 120 U. S. 287, 7 Sup. Ct. 482. Compare *New Castle Northern Ry. Co. v. Simpson*, 21 Fed. 533.

¹⁹⁰ *Stein v. Howard*, 65 Cal. 816, 4 Pac. 662. And see *Mathis v. Pridham*, 1 Tex. Civ. App. 58, 20 S. W. 1015; *Nelson v. Hubbard*, 96 Ala. 238, 11 South. 428, 432.

¹⁹¹ 103 Ill. 187.

provision in Illinois applying to railroad companies was intended to prevent reckless and unscrupulous speculators, under the guise or pretense of building a railroad or of accomplishing some other legitimate corporate purpose, from fraudulently issuing and putting upon the market bonds or stocks that do not, and are not intended to, represent money or property of any kind, either in possession or in expectancy, the stock or bonds in such case being entirely fictitious; that it was not intended to interfere with the usual and customary methods of raising funds by railroad companies by the issue of its stock or bonds, for the purpose of building their roads, or of accomplishing other legitimate corporate purposes.

Such a provision prohibits the issue of stock to subscribers on payment in cash of a less sum than its par value.¹⁹² And it has been held that it prohibits a corporation from doubling its capital stock, and distributing the new stock among the stockholders as a stock dividend on the ground that its original capital stock has been invested in property which has more than doubled in value.¹⁹³

As we have seen, the New York court has held, in the absence of constitutional or statutory prohibition, that a corporation, in issuing stock in payment of property, may issue it at its actual, instead of its par, value.¹⁹⁴ The New York statute relating to manufacturing corporations provides that on the purchase of property by such a corporation, stock may be issued "to the amount of the value of the property" in payment, and that the stock so issued shall be taken to be full-paid stock. It has been held that the statute means that the stock must be issued at its par value, though that may be greater than its market value.¹⁹⁵

In Alabama there are constitutional and statutory provisions prohibiting the issue of stock except for money or property actually received, and requiring all stock subscriptions to be paid in money, or in labor or property at its money value. Under these provisions it was said in *Elyton Land Co. v. Birmingham Warehouse & Elevator Co.*¹⁹⁶ that subscribers who pay their subscriptions in labor or prop-

¹⁹² *Williams v. Evans*, 87 Ala. 725, 6 South. 702.

¹⁹³ *Fitzpatrick v. Publishing Co.*, 83 Ala. 604, 2 South. 727.

¹⁹⁴ *Van Cott v. Van Brunt*, 82 N. Y. 535.

¹⁹⁵ *Gamble v. Water Co.*, 123 N. Y. 91, 25 N. E. 201.

¹⁹⁶ 92 Ala. 407, 9 South. 129, 1 Cumming, Cas. Priv. Corp. 870.

erty of a less money value than the amount of their subscriptions, though this is done by all the subscribers, and though there is no fraud, are liable to creditors of the corporation for the difference between the value of the property and the amount of their subscriptions. The dictum in this case goes much further than was necessary. The defendants had organized a corporation with a capital stock of \$250,000, and subscribed for the whole amount. In payment of their subscription they transferred to the company a bond for title for land for which they had paid only \$5,000. For the balance of the purchase money (about \$50,000) the company executed its notes. The land was worth no more than was paid for it. Here, therefore, was a case in which there was so great a difference between the amount of stock and the value of the property that the court could have held it to be a case of fraud in law, and the decision, on the facts, is nothing more than an application of the doctrine explained in a preceding paragraph. The New York cases under a similar provision are to the same effect.¹⁹⁷ It is not to be supposed that the Alabama court would hold a transaction by which a corporation receives property in payment for stock invalid as against creditors, where there was no actual fraud, and the overvaluation was not intentional, but was due merely to error of judgment.

Liability of Transferees.

Where stock is issued by a corporation as full paid on payment of a part only, and the person to whom it is issued transfers the same to a purchaser with notice, the transferee stands in the transferor's shoes, and will be liable on the stock to the same extent as the transferor. But, if the transfer is to a purchaser without notice, no such liability attaches. The stock, in his hands, must be regarded as full paid.¹⁹⁸ It was said by the court of appeals of Maryland in *Brant v. Ehlen*:¹⁹⁹ "The liability for subscription to the stock of a corporation is founded on contract. Where one agrees to take a certain number of shares, the law implies a promise to pay for them

¹⁹⁷ Ante, p. 381.

¹⁹⁸ *Brant v. Ehlen*, 59 Md. 1; *Du Pont v. Tilden*, 42 Fed. 87; *Steacy v. Railroad Co.*, 5 Dill. 348, Fed. Cas. No. 13,329; *Cleveland Rolling-Mill Co. v. Texas & St. L. Ry. Co.*, 27 Fed. 250; *Young v. Iron Co.*, 65 Mich. 111, 31 N. W. 814. And see *Libby v. Tobey*, 82 Me. 397, 19 Atl. 904.

¹⁹⁹ 59 Md. 1.

according to the terms of his subscription. If they are sold before all installments are paid, and are bought with such knowledge, the law implies a promise on the part of the purchaser to pay whatever may be due thereon, according to the terms of the original subscription. In such cases the purchaser stands in the shoes of the original subscriber. These are elementary principles, about which there can be no contention. But where shares are issued by the company to the subscriber as full-paid shares, and are sold by the subscriber as such, there is no ground on which a promise can be implied, on the part of the purchaser without notice, to be answerable, either to the company or to its creditors, should the representations on the faith of which he purchased prove to be false. He could not be held liable on the ground of contract, because he never agreed to purchase any other shares than full-paid shares; and, if it be said that the shares were fraudulently issued, he could not be held liable on the ground of fraud, because he was in no sense a party to the fraud." Nor can he be held liable in such a case under the doctrine that the unpaid subscriptions of an insolvent corporation constitute a trust fund for the payment of its debts, for the doctrine does not apply in such a case.²⁰⁰

ACTIONS BY STOCKHOLDERS FOR INJURIES TO CORPORATION—INTERFERENCE IN MANAGEMENT.

149. AT LAW—A stockholder cannot maintain an action at law for an injury to the corporation. Such an action can only be brought by the corporation.

150. IN EQUITY—The corporation is the proper party to sue in equity to redress or prevent wrongs against it, committed or threatened, either by strangers, or by its own officers or agents; but a court of equity will entertain such a suit by a stockholder, on behalf of himself and the other stockholders, where, for any reason, redress or protection cannot be obtained through the corporation or its officers.

²⁰⁰ Brant v. Ehlen, *supra*.

- 151. To enable a stockholder to maintain in a court of equity, in his own name, a suit founded on a right of action existing in the corporation itself, and in which the corporation itself is the proper party to sue, there must exist as the foundation of the suit:**
- (a) Some action or threatened action of the managing board of directors or trustees of the corporation which is beyond the authority conferred upon them by the charter or other source of organization.**
 - (b) Or such a fraudulent transaction completed or contemplated by the acting managers, in connection with some other party or among themselves, or with other shareholders, as will result in serious injury to the corporation, or to the interests of the other stockholders.**
 - (c) Or the board of directors or trustees, or a majority of them, must be acting for their own interests, in a manner destructive of the corporation itself, or of the rights of the other shareholders.**
 - (d) Or the majority of the stockholders themselves must be oppressively and illegally pursuing a course which is in violation of the rights of the other shareholders, and which can only be restrained by the aid of a court of equity.**
 - (e) In addition to the existence of grievances calling for equitable relief, it must appear that the complainant has exhausted all the means within his reach to obtain, within the corporation itself, the redress of his grievances. He must apply to the managing officers to take action in the corporate name; and if he fails with them, he must, if the matter will admit of the delay, seek to obtain action by the stockholders as a body, unless for some reason such attempt would be useless.**

As was explained in treating of the nature of a corporation, the corporate body exists in law as a legal entity, separate and distinct

from the members who compose it. The corporation and its members are not the same thing for the purpose of suits to redress injuries to the corporation. A corporation is a collection of individuals, it is true; but the individuals in their collective capacity are represented by the corporation, the artificial person. An infringement of their collective rights is an injury to the corporation, for which an action, if brought at all, must be brought by the corporation. For such injuries, as a general rule, the individual members cannot sue. This applies not only to injuries inflicted by strangers, but it also applies to injuries resulting from the wrongs of the officers or agents of the corporation.

Actions at Law.

It is well settled that a stockholder cannot maintain an action at law for injury to the corporation, either by its officers or by a stranger. The property of a corporation belongs to the corporation as a distinct legal entity separate from the members who compose it, and for any injury thereto the corporation must sue. Neither a single stockholder, for instance, nor even all of the stockholders, could maintain trover or trespass for conversion of or injury to the corporate property, or replevin to recover the same; but all such suits must be brought by the corporation.²⁰¹ Nor can a stockholder maintain an action at law against the directors or other officers of a corporation for their negligence or misfeasance in conducting its affairs, whereby the capital is wasted and lost, though the shares are thereby rendered worthless. Such an action, when it can be maintained at all, must be brought by the corporation, for the injury is to the corporation.²⁰² All injuries to corporate property are indirectly injurious to the stockholders, but at law their rights must invariably be asserted through the corporation. If, for any reason, the corporation will not sue for injuries suffered by it, the remedy of a stockholder, if he has any, is in equity.

²⁰¹ Ante, pp. 7, 8; *Tomlinson v. Bricklayers' Union No. 1*, 87 Ind. 308, 1 Cumming, Cas. Priv. Corp. 33; *Button v. Hoffman*, 61 Wis. 20, 20 N. W. 667, 1 Cumming, Cas. Priv. Corp. 38.

²⁰² *Smith v. Hurd*, 12 Metc. (Mass.) 871, 1 Cumming, Cas. Priv. Corp. 792; *Talbot v. Scripps*, 31 Mich. 268; *Allen v. Curtis*, 26 Conn. 456.

Suits in Equity.

It was at one time contended that a court of equity had no jurisdiction over a corporation, as such, at the suit of a stockholder for violations of its charter. But that it has such jurisdiction is now well settled. It was said by the supreme court of the United States in 1855: "It is now no longer doubted, either in England or the United States, that courts of equity, in both, have a jurisdiction over corporations, at the instance of one or more of their members, to apply preventive remedies by injunction, to restrain those who administer them from doing acts which would amount to a violation of charters, or to prevent any misapplication of their capital or profits which might result in lessening the dividends of stockholders, or the value of their shares, as either may be protected by the franchises of a corporation, if the acts intended to be done create what is in the law denominated a breach of trust. And the jurisdiction extends to inquire into, and to enjoin, as the case may require that to be done, any proceedings by individuals, in whatever character they may profess to act, if the subject of complaint is an imputed violation of a corporate franchise, or the denial of a right growing out of it, for which there is not an adequate remedy at law."²⁰³

If a case arises of injury to a corporation by some of its members, or by its officers, or by strangers, for which no adequate remedy remains except that of a suit by individual members in their private characters, asking in such character the protection of those rights to which in their corporate character they are entitled, a court of equity will regard the claims of justice as superior to any difficulties arising out of technical rules respecting the mode in which corporations are required to sue, and will entertain a suit by stockholders individually.²⁰⁴ Therefore it is well settled that if the majority of

²⁰³ Dodge v. Woolsey, 18 How. 331; 1 Cumming, Cas. Priv. Corp. 739. And see Pratt v. Pratt, Read & Co., 33 Conn. 446, 455, 2 Cumming, Cas. Priv. Corp. 219; Hartford & N. H. R. Co. v. Croswell, 5 Hill (N. Y.) 383; Stevens v. Railroad Co., 29 Vt. 545; Hardon v. Newton, 14 Blatchf. 376, Fed. Cas. No. 6,054, 1 Cumming, Cas. Priv. Corp. 487; Bacon v. Robertson, 18 How. 480, 1 Cumming, Cas. Priv. Corp. 468; Robinson v. Smith, 3 Paige (N. Y.) 222; and cases cited in note 205, *infra*.

²⁰⁴ Dictum of Vice Chancellor Wigram in Foss v. Harbottle, 2 Hare, 461, 1 Cumming, Cas. Priv. Corp. 693. And see the cases hereafter cited.

the stockholders do or threaten to do acts which are ultra vires of the corporation, or which constitute a violation of the rights of the other stockholders, and the directors cannot or will not take steps to redress or prevent the wrong, or if the directors or other officers do or threaten such acts, and the majority of the stockholders participate or acquiesce, or if a stranger inflicts an injury, and the corporate officers and majority of the stockholders fraudulently refuse to sue for redress, a stockholder, on his own behalf, or on behalf of himself and others, may maintain a suit in equity to redress or enjoin the wrong, and the suit cannot be defeated on the ground that the injury is to the corporation, and that it ought to sue.²⁰⁵ Any other rule would allow the majority to "freeze out" the minority. They could violate the rights of the minority at their pleasure, and could put all the assets of the company into their pockets; and, as they could prevent a suit by the corporation, the minority would be without any means of redress.

To entitle a stockholder to maintain a suit in equity to redress a corporate injury from an act done or to prevent a corporate injury from an act threatened, either in his own name, or on behalf of himself and other stockholders, it must be shown that every reasonable effort to obtain redress or protection through the regularly constituted agents and controlling power of the corporation has proved

²⁰⁵ *Atwood v. Merryweather*, L. R. 5 Eq. 464, note, 1 Cumming, Cas. Priv. Corp. 717; *Simpson v. Hotel Co.*, 8 H. L. Cas. 712; *Menier v. Telegraph Works*, 9 Ch. App. 350, 1 Cumming, Cas. Priv. Corp. 722; *Booth v. Robinson*, 55 Md. 419; *Mason v. Harris*, 11 Ch. Div. 97, 1 Cumming, Cas. Priv. Corp. 731; *Russell v. Waterworks Co.*, L. R. 20 Eq. 474, 1 Cumming, Cas. Priv. Corp. 725; *Dodge v. Woolsey*, 18 How. 331, 1 Cumming, Cas. Priv. Corp. 739; *Chicago City Ry. Co. v. Allerton*, 18 Wall. 233, 1 Cumming, Cas. Priv. Corp. 752; *Zabriskie v. Railroad Co.*, 23 How. 381; *City of Davenport v. Dows*, 18 Wall. 626, 1 Cumming, Cas. Priv. Corp. 754; *Hawes v. City of Oakland*, 104 U. S. 450, 1 Cumming, Cas. Priv. Corp. 756; *Nathan v. Tompkins*, 82 Ala. 437, 2 South. 747; *Peabody v. Flint*, 6 Allen (Mass.) 52, 1 Cumming, Cas. Priv. Corp. 795; *Brewer v. Boston Theatre*, 104 Mass. 378; *Miner v. Ice Co.*, 93 Mich. 97, 53 N. W. 218, 2 Cumming, Cas. Priv. Corp. 234, Shep. Cas. Corp. 181; *City of Chicago v. Cameron*, 120 Ill. 447, 11 N. E. 899; *Bailey v. Gaslight Co.*, 27 N. J. Eq. 196, 2 Cumming, Cas. Priv. Corp. 207; *Wayne Pike Co. v. Hammons*, 129 Ind. 368, 27 N. E. 487; *Allen v. Curtis*, 26 Conn. 456; *Slattery v. Transportation Co.*, 91 Mo. 217, 4 S. W. 79; *Greaves v. Gouge*, 69 N. Y. 154; *Brinckerhoff v. Bostwick*, 88 N. Y. 52; *Black v. Huggins*, 2 Tenn. Ch. 780; *Cogswell v. Bull*, 39 Cal. 320; *Hazard v. Durant*, 11 R. I. 195.

unavailing. It must be made to appear from the bill, not only that the directors are disabled, by their disqualification or misconduct, to sue, or that they have wrongfully refused to do so upon a proper demand; but, where the matter will admit of the necessary delay, and it is practicable to call upon the stockholders to act, it must also be shown that this has been done.²⁰⁶ No doctrine in the law of corporations is better settled than this. The only difficulty is in its application to particular cases. It is not enough to show inability or refusal to sue on the part of the directors, but it must be shown that for some reason redress cannot be obtained by calling a meeting of the stockholders, who would have the power to direct suit to be brought in the name of the corporation, and to remove the offending directors and elect others who would institute the suit.²⁰⁷

When the directors or officers of a corporation cause a loss of corporate property by negligence or culpable lack of prudence or failure to exercise their functions; or fraudulently misappropriate the corporate property in any manner, whether for their own benefit or for the benefit of a third person; or obtain any undue advantage, benefit, or profit for themselves by contract, purchase, sale, or other dealings under color of their official functions; or misuse the franchise; or violate the rules established by the charter or by-laws for their management of the corporate affairs; or in any other similar manner commit a breach of their fiduciary obligations towards the corporation, so that it sustains injury or loss, and a liability devolves upon themselves,—then the corporation is the party to sue for equitable relief, and in such cases no equitable suit for relief can be maintained against the directors or officers by the stockholder or stock-

²⁰⁶ *Foss v. Harbottle*, 2 Hare, 461, 1 Cumming, Cas. Priv. Corp. 693; *Moxley v. Alston*, 1 Phil. Ch. 790; *Russell v. Waterworks Co.*, L. R. 20 Eq. 474, 1 Cumming, Cas. Priv. Corp. 725; *Hawes v. City of Oakland*, 104 U. S. 450, 1 Cumming, Cas. Priv. Corp. 756; *Allen v. Wilson*, 28 Fed. 677; *Booth v. Robinson*, 55 Md. 419; *Brewer v. Boston Theatre*, 104 Mass. 378; *Dunphy v. Association*, 146 Mass. 495, 16 N. E. 426, 1 Cumming, Cas. Priv. Corp. 769; *Mount v. Trust Co. (Va.)* 25 S. E. 244; *Rathbone v. Gas Co.*, 31 W. Va. 798, 8 S. E. 570; *Hersey v. Veazie*, 24 Me. 9; *Greaves v. Gouge*, 69 N. Y. 154; *Doud v. Railway Co.*, 65 Wis. 108, 25 N. W. 533; *Hazard v. Durant*, 11 R. I. 195; *Black v. Huggins*, 2 Tenn. Ch. 780; *Cogswell v. Bull*, 39 Cal. 320.

²⁰⁷ *Foss v. Harbottle*, 2 Hare, 461, 1 Cumming, Cas. Priv. Corp. 693; *Moxley v. Alston*, 1 Phil. Ch. 790; *Rathbone v. Gas Co.*, 31 W. Va. 798, 8 S. E. 570.

holders individually, nor by a stockholder in a representative capacity on behalf of all the others similarly situated, unless the corporation either actually or virtually refuses to prosecute.²⁰⁸

The effort by a stockholder to induce the managing body of the corporation to sue must have been earnest, and not simulated.²⁰⁹ No request at all to sue need be made of the directors, nor of the stockholders as a body, if it is clear that the request would be useless.²¹⁰ Thus, when the president of a corporation was its general manager, and owned a majority of the stock, it was held that a demand upon him to sue, and his refusal, was sufficient to entitle a stockholder to sue in his own name to have construction bonds of the company, unlawfully issued by the president, declared ultra vires and void.²¹¹ A stockholder, complaining of misconduct of the treasurer of a corporation, is not excused from applying to the directors to bring suit, before bringing it himself, by the fact that the treasurer owns the majority of the stock; but this fact does excuse him from applying to a stockholders' meeting.²¹² It is not enough, to excuse application to the directors or stockholders as a body, to show that they would probably refuse to take steps to obtain relief.²¹³

Acts within the Power of the Majority—Discretionary Powers.

"Nothing connected with internal disputes between shareholders is to be made the subject of a bill by some one shareholder on behalf of himself and others, unless there be something illegal, oppressive, or fraudulent; unless there is something ultra vires on the part of the company qua company, or on the part of the majority of the company, so that they are not fit persons to determine it; but every litigation must be in the name of the company, if the company really

²⁰⁸ Doud v. Railway Co., 65 Wis. 108, 25 N. W. 533.

²⁰⁹ Bacon v. Irvine, 70 Cal. 221, 11 Pac. 648; Dannmeyer v. Coleman, 11 Fed. 97; Hawes v. City of Oakland, 104 U. S. 450, 1 Cumming, Cas. Priv. Corp. 756; City of Detroit v. Dean, 106 U. S. 537, 1 Sup. Ct. 560.

²¹⁰ City of Chicago v. Cameron, 120 Ill. 447, 11 N. E. 899; Mack v. Iron Co., 90 Ala. 396, 8 South. 150; Starbuck v. Trust Co. (Shepaug Voting Trust Cases) 60 Conn. 553, 24 Atl. 32.

²¹¹ City of Chicago v. Cameron, supra.

²¹² Dunphy v. Association, 146 Mass. 495, 16 N. E. 426, 1 Cumming, Cas. Priv. Corp. 769. And see Allen v. Wilson, 28 Fed. 677.

²¹³ Foote v. Mining Co., 17 Fed. 46.

desire it.”²¹⁴ Obviously a stockholder, or a minority of the stockholders, cannot maintain a suit to prevent or to set aside a transaction by the majority, if the transaction is within the powers of the majority. In such a case the will of the majority must govern, and the courts will not interfere merely because a minority of the stockholders object to the transaction, and deem it injurious to the interests of the corporation. As was said by the Kentucky court, in a suit for an injunction, relief will not be granted unless the corporation, represented by the majority, is about to do some act outside of the scope of its authority, or in disobedience to the provisions of its constitution; for so long as it exercises the powers granted by the charter the acts of the company must be treated by the courts as the acts of all the stockholders. Each and every stockholder contracts that the will of the majority shall govern in all matters coming within the limits of the act of incorporation; and in cases involving no breach of trust, but only error or mistake of judgment upon the part of the directors who represent the company, individual stockholders have no right to appeal to the courts to dictate the line of policy to be pursued by the corporation.²¹⁵

If the majority of the stockholders are abusing their powers, and are depriving the minority of their rights, the minority may, in a proper case, come into a court of equity, and sue in their own names to maintain their rights. But they cannot sue to set aside something which the majority were entitled to do, though it may have been done irregularly. “If the thing complained of is a thing which, in substance, the majority of the company are entitled to do, or if something has been done irregularly which the majority of the company are entitled to do regularly, or if something has been done illegally which the majority of the company are entitled to do legally,” the court will not interfere at the suit of individual stockholders.²¹⁶

²¹⁴ *Macdougall v. Gardiner*, 1 Ch. Div. 13, 1 Cumming, Cas. Priv. Corp. 704.

²¹⁵ *Dudley v. High School*, 9 Bush (Ky.) 576, 1 Cumming, Cas. Priv. Corp. 767. And see *Foss v. Harbottle*, 2 Hare, 461, 1 Cumming, Cas. Priv. Corp. 693; *Durfee v. Railroad Co.*, 5 Allen (Mass.) 230, 1 Cumming, Cas. Priv. Corp. 773; *Bill v. Telegraph Co.*, 16 Fed. 14. See ante, p. 351, for the application of this principle to suits by stockholders to compel the corporation to declare and pay a dividend.

²¹⁶ *Macdougall v. Gardiner*, 1 Ch. Div. 13, 1 Cumming, Cas. Priv. Corp. 704. Per Mellish, L. J.

It has been held, under this doctrine, that a stockholder in a corporation, the charter of which is subject to amendment or repeal at the pleasure of the legislature, cannot maintain a suit to restrain the corporation from engaging in a new enterprise, in addition to that contemplated by the charter, but of the same kind, if it is sanctioned by an express legislative grant, and by a vote of the majority of the stockholders.²¹⁷ As to this proposition, however, there is much doubt. Perhaps the weight of authority is against it.²¹⁸

A stockholder, or a minority of the stockholders, cannot maintain a suit to set aside a transaction entered into by the directors fraudulently or in excess of their authority, if it is one which a majority of the stockholders may lawfully ratify, and thus render binding as against the minority. In *Foss v. Harbottle*²¹⁹ the complaint in a suit by stockholders was that the directors had fraudulently purchased land from themselves for the corporation at an excessive price. Vice Chancellor Wigram held that the suit could not be maintained, since the transaction, though subject to rescission by the corporation, was not void, but might be ratified by a majority of the members.²²⁰

Even when it is clear that a corporation has a right to sue to redress or enjoin wrongs committed or threatened, the fact that it refuses to do so does not necessarily entitle a stockholder to sue on behalf of himself and the other stockholders. As a rule, the courts will not interfere at the suit of a stockholder to obtain redress for an injury to the corporation, because of failure or refusal of the directors, or of the majority of the stockholders, to sue. It is only when the action of the corporation in refusing to proceed at the request of a stockholder is fraudulent as against him, or in disregard of his rights, that he can maintain a suit in his own name in the corporate right. The court cannot interfere with the management of corporations in matters which are properly within their discretion, so long as their discretion is fairly exercised; and it is always assumed,

²¹⁷ *Durfee v. Railroad Co.*, 5 Allen (Mass.) 230, 1 Cumming, Cas. Priv. Corp. 773.

²¹⁸ Compare *Zabriskie v. Railroad Co.*, 18 N. J. Eq. 178, 1 Cumming, Cas. Priv. Corp. 781. See ante, p. 331, and post, p. 447, where the cases are referred to.

²¹⁹ 2 Hare, 461, 1 Cumming, Cas. Priv. Corp. 698.

²²⁰ And see *Bill v. Telegraph Co.*, 16 Fed. 14.

until the contrary appears, that they and their officers obey the law, and act in good faith towards all their members.²²¹ It is generally discretionary with a corporation whether it will sue for injuries suffered by it; and, so long as it acts fairly in refusing to sue, the courts will not entertain a suit by an individual stockholder. "It is not always best to insist upon all one's rights; and a corporation, acting by its directors, or by vote of its members, may properly refuse to bring a suit which one of its stockholders believes should be prosecuted. In such a case the will of the majority must control."²²²

The Rule as Stated by the United States Supreme Court.

In *Hawes v. City of Oakland*²²³ the supreme court of the United States thus states the doctrine governing suits by stockholders:

"We understand that doctrine to be that, to enable a stockholder in a corporation to sustain in a court of equity, in his own name, a suit founded on a right of action existing in the corporation itself, and in which the corporation itself is the appropriate plaintiff, there must exist, as the foundation of the suit:

"Some action or threatened action of the managing board of directors or trustees of the corporation which is beyond the authority conferred on them by their charter or other source of organization;

"Or such a fraudulent transaction, completed or contemplated, by the acting managers, in connection with some other party, or among themselves, or with other shareholders, as will result in serious injury to the corporation, or to the interests of the other shareholders;

"Or where the board of directors, or a majority of them, are acting

²²¹ Per Knowlton, J., in *Dunphy v. Association*, 146 Mass. 495, 16 N. E. 426, 1 Cumming, Cas. Priv. Corp. 769.

²²² *Dunphy v. Association*, supra. "There may be a great many wrongs committed in a company,—there may be claims against directors, there may be claims against officers, there may be claims against debtors; there may be a variety of things which a company may well be entitled to complain of, but which, as a matter of good sense, they do not think it right to make the subject of litigation; and it is the company, as a company, which has to determine whether it will make anything that is a wrong to the company a subject-matter of litigation, or whether it will take steps to prevent the wrong from being done." Per Sir W. M. James, L. J., in *Macdougall v. Gardiner*, 1 Ch. Div. 13, 1 Cumming, Cas. Priv. Corp. 704.

²²³ 104 U. S. 450, 1 Cumming, Cas. Priv. Corp. 756. And see *Dimpfell v. Ohio & M. R. Co.*, 110 U. S. 209, 3 Sup. Ct. 573, 1 Cumming, Cas. Priv. Corp. 765.

for their own interest, in a manner destructive of the corporation itself, or of the rights of the other shareholders;

"Or where the majority of shareholders themselves are oppressively and illegally pursuing a course in the name of the corporation, which is in violation of the rights of the other shareholders, and which can only be restrained by the aid of a court of equity.

"Possibly other cases may arise in which, to prevent irremediable injury, or a total failure of justice, the court would be justified in exercising its powers; but the foregoing may be regarded as an outline of the principles which govern this class of cases.

"But, in addition to the existence of grievances which call for this kind of relief, it is equally important that, before the shareholder is permitted in his own name to institute and conduct a litigation which usually belongs to the corporation, he should show to the satisfaction of the court that he has exhausted all the means within his reach to obtain, within the corporation itself, the redress of his grievances, or action in conformity to his wishes. He must make an earnest, not a simulated, effort with the managing body of the corporation to induce remedial action on their part, and this must be made apparent to the court. If time permits, or has permitted, he must show, if he fails with the directors, that he has made an honest effort to obtain action by the stockholders as a body in the matter of which he complains. And he must show a case, if this is not done, where it could not be done, or it was not reasonable to require it."

Laches and Estoppel.

A stockholder may be precluded by acquiescence, laches, or estoppel from bringing suit to redress injuries to the corporation by the directors, or other officers, or by the majority of the stockholders, or by third persons; for such suits are subject to the familiar principle of equity jurisprudence that acquiescence in a course of conduct by one interested in it, especially when the rights of others are affected thereby, will induce the court to refuse him relief.²²⁴ Thus it was

²²⁴ *Dunphy v. Association*, 146 Mass. 495, 16 N. E. 426, 1 Cumming, Cas. Priv. Corp. 769; *Dimpfell v. Railway Co.*, 110 U. S. 209, 3 Sup. Ct. 573, 1 Cumming, Cas. Priv. Corp. 765; *Allen v. Wilson*, 28 Fed. 677; *Boyce v. Coal Co.*, 37 W. Va.

held in a late Massachusetts case that a stockholder could not bring suit for improper investments of corporate funds, made three years before, if he knew of them at the time, and did not object.²²⁵ And it has often been held that a stockholder is estopped to object to corporate acts done with his consent.²²⁶

Motive of Stockholder.

Ordinarily, the motive of a stockholder in suing to restrain ultra vires acts by the corporation is immaterial. But he must come in a bona fide character as a stockholder. In *Forrest v. Manchester S. & L. Ry. Co.*,²²⁷ the plaintiff, who held a small amount of stock in the defendant company, sued to enjoin acts alleged to be ultra vires. It appeared that the other stockholders were opposed to the suit, and that another corporation, in which the plaintiff was a larger stockholder, directed him to institute it, and had indemnified him against costs, and that the suit was really in the interests of this company. It was held, without deciding whether the acts complained of were ultra vires, that the suit, not being instituted by the plaintiff in a bona fide character as a stockholder, was an imposition on the court, and could not be maintained.²²⁸

Parties to Suits.

A suit in equity by a stockholder to redress or enjoin injuries to the corporation can only be maintained on the ground that the rights of the corporation are involved; and the suit should be so conducted that any decree on the merits will be binding upon the corporation. It is therefore necessary to make the corporation a party defendant. It would be wrong, in case the stockholder were unsuccessful in his suit, to allow the corporation to renew the litigation in another suit; and to avoid this result a court of equity will not take cognizance of

78, 16 S. E. 501; *Alexander v. Searcy*, 81 Ga. 536, 8 S. E. 630; *Peabody v. Flint*, 6 Allen (Mass.) 54; *Gregory v. Patchett*, 33 Beav. 595; *Ashurst's Appeal*, 60 Pa. St. 290; *Watt's Appeal*, 78 Pa. St. 370; *Stewart v. Transportation Co.*, 17 Minn. 372 (Gil. 348).

²²⁵ *Dunphy v. Association*, *supra*.

²²⁶ See the cases cited above.

²²⁷ 4 De Gex, F. & J. 125, 1 Cumming, Cas. Priv. Corp. 713.

²²⁸ And see *Waterbury v. Express Co.*, 50 Barb. (N. Y.) 157.

a bill brought to settle a question in which the corporation is the essential party in interest, unless it be made a party to the suit.²²⁹

Where the subject-matter of the complaint is fraud or misconduct on the part of the directors or other officers of the corporation, they also must be made defendants.²³⁰

If the subject-matter of the suit is an agreement between the corporation, acting by its directors or managers, and some other corporation, or some other person, strangers to the corporation, it is proper to make that other corporation or person a defendant to the suit; and the court may grant relief against such corporation or person, as by compelling it to return money or property received under the agreement, if it was ultra vires or fraudulent.²³¹

EXPULSION OF MEMBERS.

152. Corporations not having a joint stock have, as an incident, power to remove or expel members for sufficient cause. This right does not exist in joint-stock corporations. When the charter is silent on the subject, or grants the power in general terms, it can be exercised only for the following causes:

- (a) Offenses of an infamous character, and indictable at common law, and of which the party has been convicted.**
- (b) Offenses against the party's duty to the corporation as a member of it.**
- (c) Offenses compounded of these two.**

A joint-stock corporation has no power to remove or expel its stockholders, unless the power to do so is expressly conferred upon

²²⁹ *Davenport v. Dows*, 18 Wall. 626, 1 Cumming, Cas. Priv. Corp. 754. And see *Hersey v. Veazie*, 24 Me. 9; *Greaves v. Gouge*, 69 N. Y. 134; *Black v. Huggins*, 2 Tenn. Ch. 780; *Brinckerhoff v. Bostwick*, 88 N. Y. 52; *Allen v. Curtis*, 28 Conn. 456; *Mount v. Trust Co. (Va.)* 25 S. E. 244.

²³⁰ *Slattery v. Transportation Co.*, 91 Mo. 217, 4 S. W. 79.

²³¹ *Russell v. Wakefield Waterworks Co.*, L. R. 20 Eq. 474, 1 Cumming, Cas. Clk.Pr.Corp.—26

it by its charter or by agreement with its members.²³² In the case of other corporations, however, they have the power to remove members for good cause, provided they do not thereby violate charter or statutory provisions. This power need not be expressly conferred by the charter. It is an incident to every corporation other than a joint-stock corporation.²³³ Questions as to the nature and extent of this power have frequently arisen in connection with incorporated clubs, literary and medical societies, benevolent societies, boards of trade, etc.

The power can only be exercised for good cause, and it must be for some offense that has an immediate relation to the duties of the party as a member, or for an offense of an infamous character, indictable at law, and of which the party has been convicted. And a by-law or rule authorizing expulsion for a less cause is void.²³⁴ "It appears to be well settled that when the charter of a corporation is silent upon the subject of expulsion, or grants the power in general terms, there are but three legal causes of disfranchisement: (1) Offenses of an infamous character indictable at common law. (2) Offenses against the corporator's duty to the corporation as a member of it. (3) Offenses compounded of the two."²³⁵

A member may be expelled from a board of trade for violating a rule prohibiting members, under penalty of expulsion, from making any contract for the future delivery of produce before the time fixed for opening the exchange room, or after the time fixed for closing the same;²³⁶ or from making or reporting any false or fictitious purchase

Priv. Corp. 725; *Salomons v. Laing*, 12 Beav. 377; *Peabody v. Flint*, 6 Allen (Mass.) 52, 57, 1 Cumming, Cas. Priv. Corp. 795.

²³² See *Edgerton Tobacco Manuf'g Co. v. Croft*, 69 Wis. 256, 34 N. W. 143; *Pulford v. Fire Department*, 31 Mich. 465.

²³³ 2 Kent, Comm. 297; 1 Thomp. Corp. 847; *Lord Bruce's Case*, 2 Strange, 819; *Rex v. Richardson*, 1 Burrows, 517; *Dickenson v. Chamber of Commerce*, 29 Wis. 45; *Fawcett v. Charles*, 13 Wend. (N. Y.) 473.

²³⁴ 2 Kent, Comm. 297; *Com. v. Society*, 2 Binn. (Pa.) 441; *New York Protective Ass'n v. McGrath* (Super. N. Y.) 5 N. Y. Supp. 8; *Otto v. Union*, 75 Cal. 308, 17 Pac. 217.

²³⁵ *State v. Chamber of Commerce*, 20 Wis. 63, 71; *Dickenson v. Chamber of Commerce*, 29 Wis. 45; *Evans v. Philadelphia Club*, 50 Pa. St. 107. See 1 Thomp. Corp. §§ 849-876, collecting the cases.

²³⁶ *State v. Chamber of Commerce*, 47 Wis. 670, 3 N. W. 760.

or sale, or from acting in bad faith or dishonestly.²³⁷ So a by-law of a board of trade or similar corporation may authorize expulsion of a member for nonfulfillment of any contract.²³⁸

On the other hand, it has been held that a by-law of a benevolent society, authorizing expulsion of a member for vilifying any of the other members, is void, as such conduct does not affect the interest or good government of the corporation, and is not indictable by the law of the land.²³⁹

If a member is guilty of an offense which renders him liable to indictment, but which has no immediate relation to the corporation or his duties as a member, he cannot be expelled therefor until his guilt is established by an indictment and trial at law.²⁴⁰

If there is no special provision on the subject in the charter, the power of removal of a member for cause is in the whole body, and not in the board of managers or other officers.²⁴¹ But a select body of the corporation, as the board of directors may possess the power, not only when it is given by the charter, but in consequence of a by-law made by the body at large, for the body at large may thus delegate the power to its agents or managing body.²⁴²

Strictly speaking, the term "a motion" applies only to officers. "Disfranchisement" is the term applied to the removal or expulsion of members.²⁴³

"It is absolutely essential to the validity of the suspension or expulsion of a member of an incorporated society that the accused should be notified of the charges against him, and of the time and place set for their hearing; that the accusing body should proceed

²³⁷ *Pitcher v. Board of Trade*, 121 Ill. 412, 13 N. E. 187.

²³⁸ *Dickenson v. Chamber of Commerce*, 29 Wis. 45.

²³⁹ *Com. v. Society*, 2 Binn. (Pa.) 441.

²⁴⁰ 2 Kent, Comm. 297; *Com. v. St. Patrick's Society*, 2 Binn. (Pa.) 441.

²⁴¹ 2 Kent, Comm. 298; *State v. Chamber of Commerce*, 20 Wis. 63.

²⁴² 2 Kent, Comm. 298; *Pitcher v. Board of Trade*, 121 Ill. 412, 13 N. E. 187; *State v. Chamber of Commerce*, 47 Wis. 670, 3 N. W. 760. Where one appears before the board of directors of an association charged with violating its rules, and submits his case to them without objection to the manner in which the body is constituted, or the mode of its proceeding, all irregularities therein are deemed to be waived. *Pitcher v. Board of Trade*, *supra*.

²⁴³ 2 Kent, Comm. 298.

upon inquiry, and consequently upon evidence; and that the accused should have a fair opportunity of being heard in his defense."²⁴⁴ And, generally, there must be a regular sentence of expulsion.²⁴⁵ These rules do not apply to mutual benefit corporations whose charter or by-laws provide that nonpayment of an assessment after notice shall, ipso facto, work a forfeiture of membership or of the member's benefit certificate.²⁴⁶ Nor does the rule quoted apply where the member becomes a nonresident, so that it is impracticable to give him notice.²⁴⁷

In expelling members the corporation or its authorized board acts in a quasi judicial character, and, so long as it confines itself to the exercise of the powers vested in it, and in good faith pursues the method prescribed by its laws, such laws not being in violation of the laws of the land, or any inalienable right of the member, its sentence is conclusive, like that of a judicial tribunal.²⁴⁸ The courts, however, will decide whether there were sufficient grounds for expulsion, and whether the power has been lawfully exercised, and they will interfere with the sentence if there was not sufficient cause for expulsion; or if the decision arrived at was contrary to natural justice; as where the member was not given an opportunity to be heard, or if the rules of the company were not observed, or if the action of the company was malicious, and not bona fide.²⁴⁹

If a member of a corporation is wrongfully expelled, and denied rights of membership, mandamus is a proper remedy to compel his reinstatement.²⁵⁰ In some states the remedy by injunction is allowed, while in others it is denied, generally, on the ground that there is an

²⁴⁴ 1 *Thomp. Corp.* § 881. See *Id.* §§ 882-899.

²⁴⁵ 1 *Thomp. Corp.* § 898.

²⁴⁶ 1 *Thomp. Corp.* §§ 881, 898.

²⁴⁷ 1 *Thomp. Corp.* § 881.

²⁴⁸ *Otto v. Union*, 75 Cal. 308, 17 Pac. 217; *Com. v. Pike Beneficial Soc.*, 8 Watts & S. (Pa.) 250; *Burt v. Lodge*, 66 Mich. 85, 33 N. W. 13; *Robinson v. Lodge*, 86 Ill. 598; *Pitcher v. Board of Trade*, 121 Ill. 412, 13 N. E. 187.

²⁴⁹ *Otto v. Union*, *supra*; *Savannah Cotton Exchange v. State*, 54 Ga. 668; and cases cited in notes 234, 235, 239, 240, *supra*.

²⁵⁰ 1 *Thomp. Corp.* § 904; *State v. Chamber of Commerce*, 20 Wis. 63; *State v. Milwaukee Chamber of Commerce*, 47 Wis. 670, 3 N. W. 760; *Otto v. Union*,

adequate remedy at law by mandamus.²⁵¹ The regularity of the proceedings and the sufficiency of the evidence in case of expulsion of a member after notice, trial, and conviction cannot be inquired into collaterally.²⁵²

75 Cal. 308, 17 Pac. 217; *Black & White Smiths' Society v. Vandyke*, 2 Whart. (Pa.) 309.

²⁵¹ 1 Thomp. Corp. §§ 909-913.

²⁵² *Black & White Smiths' Society v. Vandyke*, 2 Whart. (Pa.) 309.

CHAPTER XII.

MEMBERSHIP IN CORPORATIONS (Continued).

- 153-154. Transfer of Shares.
- 155. Effect of Transfer.
- 156. Lien of Corporation on Shares.
- 157-158. Validity of Transfers.
- 159-160. Mode of Transfer.
- 161-162. Registration of Transfer.
- 163-166. Forged and Unauthorized Transfers.
- 167. Liability of Indorser of Forged Certificate.
- 168-169. Liability of Corporation Arising from Unauthorized or Invalid Transfer.
- 170-171. Liability of Corporation on Certificates Issued Fraudulently, without Authority, etc.
- 172. Remedy against Corporation for Refusal to Recognize Transfer.
- 173. Compelling Corporation to Issue New Certificates.

TRANSFER OF SHARES.

- 153. Except in so far as they may be restricted by charter or statutory provisions, or by an authorized by-law, stockholders have an absolute right to transfer their shares in good faith to any one who is capable in law of taking and holding the same, and of assuming liability in respect thereto; and this right is in no way dependent upon the consent of the corporation or of its officers or the other stockholders.
- 154. An agreement between the stockholders of a corporation not to sell, pledge, or transfer their shares is in unreasonable restraint of trade, and void.

By the charters of private corporations, the shares of stock are often expressly declared to be transferable by the holders, but express provision is not at all necessary to give the right of transfer. It exists at common law. In ordinary partnerships, as we have seen, the consent of all the partners to the admission or retirement of a

member is necessary, and every such change in membership involves the dissolution of the old firm and the formation of a new one. In corporations, however, it is different. One of the very objects of incorporation is to avoid this doctrine of the law of partnership. In the absence of express statutory restrictions, it is always implied that shares of stock are transferable. Subject to the limitations hereafter shown, it is well settled that a stockholder has an absolute right, incident to his ownership, to make an actual and bona fide sale and transfer of his shares to any person who is capable in law of taking and holding them, and of assuming liability as a stockholder. And, in the absence of express restrictions in the charter or in some statute, the right is not in any way dependent upon the consent of the directors or of the other stockholders. Unless the power to do so is expressly conferred by the legislature creating the corporation, or by an authorized amendment of its charter, neither the directors nor a majority of the stockholders can, directly or indirectly, prohibit or refuse to recognize bona fide transfers.¹ For instance, a by-law, not expressly authorized by the legislature, to the effect that the validity of a transfer shall depend upon the approval and acceptance of the board of directors, while it may perhaps be lawfully enforced to protect the rights of the corporation, and prevent transfers to irresponsible persons, cannot be enforced so as to defeat the rights of a bona fide and responsible purchaser of shares. "Its enforcement," said the Iowa court, "would operate as an infringement upon the property rights of others, which the law will not permit. It would, besides, operate as a restraint upon the disposition of property in the stock of the corporation, in the nature of restraint of trade, which the courts will not tolerate."²

A provision in the charter of a corporation that the shares shall be transferable on the books of the corporation in such manner as the

¹ *Johnson v. Laffin*, 5 Dill. 65, Fed. Cas. No. 7,393, 1 Cumming, Cas. Priv. Corp. 608, affirmed 103 U. S. 800; *Farmers' & Merchants' Bank v. Wasson*, 48 Iowa, 336; *Moore v. Bank*, 52 Mo. 377; *Bank v. Lanier*, 11 Wall. 369; *Weston's Case*, 4 Ch. App. 20; *Gilbert's Case*, 5 Ch. App. 559; *Driscoll v. Manufacturing Co.*, 59 N. Y. 96; *Bank of Attica v. Manufacturers' & Traders' Bank*, 20 N. Y. 501; *Chouteau Spring Co. v. Harris*, 20 Mo. 383.

² *Farmers' & Merchants' Bank v. Wasson*, 48 Iowa, 336. And see post, p. 457, and cases there cited.

directors shall provide, as is provided in the national banking act, is merely for the purpose of enabling the corporation to know who are stockholders, and, as such, entitled to vote, receive dividends, etc., and for the protection of bona fide purchasers of shares, and of creditors and persons dealing with the corporation, and does not in any way restrict the right of the stockholders to sell and transfer their shares, or clothe the corporation or its officers with the power to refuse to register bona fide transfers.³

Power to refuse to assent to or register a transfer, or power to prescribe the manner of transfer, is often given to the directors by the act of incorporation. Even in such a case, however, the power must be exercised in a reasonable manner and bona fide, and there must be some good reason for refusing to recognize or register a transfer. "The power," said Mr. Justice Field, "can only go to the extent of prescribing conditions essential to the protection of the association against fraudulent transfers, or such as may be designed to evade the just responsibility of the stockholder. It is to be exercised reasonably. Under the pretense of prescribing the manner of the transfer, the association cannot clog the transfer with useless restrictions, or make it dependent upon the consent of the directors or other stockholders."⁴ Power given by the charter to regulate transfers does not give the power to restrain transfers, or prescribe to whom they may be made, but merely gives the power to prescribe formalities to be observed in making them.⁵ The mere fact that the purchaser of shares is a business rival of the corporation, and hostile to it, does not affect his rights as transferee, and is no ground for refusal of a court of equity to compel the corporation to register the transfer.⁶

The directors of a corporation have the same right as any other stockholder to make a bona fide sale and transfer of their shares, and thus get rid of liability, if they comply with the regulations, and take no advantage of their position to commit fraud.⁷ There is nothing

³ Johnson v. Lafin, 5 Dill. 65, Fed. Cas. No. 7,393, 1 Cumming, Cas. Priv. Corp. 608, affirmed 103 U. S. 800.

⁴ Johnson v. Lafin, *supra*, and cases there cited and referred to.

⁵ Chouteau Spring Co. v. Harris, 20 Mo. 383.

⁶ Rice v. Rockefeller, 134 N. Y. 174, 31 N. E. 907, 2 Cumming, Cas. Priv. Corp. 181.

⁷ Johnson v. Lafin, *supra*; Gilbert's Case, 5 Ch. App. 559; Ex parte Littledale, 9 Ch. App. 257.

to prevent a transfer to an officer of the corporation, as the president or a director; and, if the transfer is in good faith, it will prevail as against any claim of the corporation against the transferror, unless there is some charter or statutory provision to the contrary.⁸

The stockholders in a corporation cannot make a valid agreement among themselves not to transfer their shares. Such an agreement, being in unreasonable restraint of trade, would be contrary to public policy, and void. In *Fisher v. Bush*⁹ a number of stockholders entered into an agreement for the expressed purpose of mutual protection, and to prevent a sale of the company's franchise by a majority of the members of the board of directors, who represented a minority of the shares, by which they agreed not to "sell, assign, set over, pledge, or give power of attorney to vote" their stock, without the consent of all the parties to the agreement. The agreement was held void because, for one reason, it was in restraint of trade and against public policy.

EFFECT OF TRANSFER.

155. By the weight of authority, when a valid and complete transfer of shares is made in good faith, and in accordance with the principles to be explained in subsequent sections, and there are no charter or statutory provisions to the contrary, the transferee takes the place of the transferror as a stockholder, and acquires all the rights and assumes all the liabilities which arise after the transfer by virtue of the shares. In detail:

(a) The transferror—

- (1) In most jurisdictions, is not liable for calls made after the transfer; but he is liable for calls previously made.
- (2) As a rule, he is no longer subject to liability as a stockholder to creditors of the corporation.
- (3) In the absence of a special agreement with the transferee, which must be known to the cor-

⁸ *Farmers' & Merchants' Bank v. Wasson*, 48 Iowa, 336.

⁹ 35 Hun (N. Y.) 641.

poration to be binding upon it, he is not entitled to dividends declared after the transfer, though earned before; but he is entitled to dividends declared before the transfer, though not paid nor payable until afterwards.

- (4) He is not entitled, after the transfer, to vote at stockholders' meetings, or otherwise take any part in the management of the corporation.

(b) The transferee

- (1) Is liable for calls made after the transfer.
- (2) He is, in most jurisdictions, liable to the same extent as the other stockholders to creditors of the corporation, though their claims may have arisen before the transfer.
- (3) He is entitled to all dividends declared after the transfer, though earned before, in the absence of an agreement to the contrary with the transferror, known to the corporation.
- (4) He is entitled to vote at stockholders' meetings, and to all other rights arising after the transfer by virtue of ownership of shares.

We shall consider in subsequent sections the manner of making a transfer of shares, and the validity of transfers. In this section will be considered generally the effect of transfers, assuming that they are valid and complete. Whenever a valid and effectual transfer is made, the effect is, in general, to substitute the transferee in the place of the transferror as a member of the corporation, and to give him all the rights, and subject him to all the liabilities, arising after the transfer, to which the transferror would have been entitled or subject if the transfer had not been made.

Liability for Calls.

If the stock is not fully paid up at the time of the transfer, the transferror, by the weight of authority, is not liable for calls subsequently made, unless he is made so by express charter or statutory provisions, or by special agreement; but the liability for such calls is

impliedly assumed by the transferee.¹⁰ In Pennsylvania the rule is different;¹¹ and by statute in some states, as in Virginia, the transferrors as well as the transferees of stock that is not fully paid are each made liable for any installment which may have accrued before the transfer or which may accrue afterwards.¹² The rule does not apply where the shares were issued as full paid, and the transferee is a bona fide purchaser. In such a case he is not liable for calls.¹³ For all calls made prior to the transfer, though not payable until afterwards, the transferror, and not the transferee, is liable.¹⁴ But, if such calls are not paid by the transferror, new calls may be made upon the transferee, leaving him to his remedy against the transferror.¹⁵ After a transfer has been made in such a manner as to be effective as

¹⁰ 1 Mor. Priv. Corp. §§ 159-161; *Isham v. Buckingham*, 49 N. Y. 216; *Webster v. Upton*, 91 U. S. 65; *Pullman v. Upton*, 96 U. S. 328; *Huddersfield Canal Co. v. Buckley*, 7 Term R. 36, 1 Cumming, Cas. Priv. Corp. 906; *Hartford & N. H. R. Co. v. Boorman*, 12 Conn. 530; *Merrimac Min. Co. v. Bagley*, 14 Mich. 501; *Bend v. Bank Co.*, 6 Har. & J. (Md.) 128, 132; *Hall v. Insurance Co.*, 5 Gill (Md.) 484, 497; *Allen v. Railroad Co.*, 11 Ala. 437.

¹¹ In Pennsylvania it is held that an original subscriber to the stock of a corporation is not discharged from liability for the amount remaining unpaid on the subscription by transferring his shares in good faith to another, unless the corporation consents to release him. See *Everhart v. Railroad Co.*, 28 Pa. St. 339; *Pittsburgh & C. R. Co. v. Clarke*, 29 Pa. St. 146; *Graff v. Railroad Co.*, 31 Pa. St. 489; *Messersmith v. Bank*, 96 Pa. St. 440. To release the transferror, in Pennsylvania, he must be released and the transferee accepted by the corporation. It is not enough for the corporation to consent to the transfer and register the same. *Messersmith v. Bank*, *supra*. The transferee is not liable in Pennsylvania for future calls, unless made so by express agreement or by statute. "No implication of a personal promise of the transferee to pay assessments arises. The company can indemnify themselves only by a sale of the stock, and pursuit of the original subscriber." *Franks Oil Co. v. McCleary*, 63 Pa. St. 317. And see *Palmer v. Mining Co.*, 34 Pa. St. 288. The rule in Ohio seems to be the same as in Pennsylvania. See *Gaff v. Flesher*, 33 Ohio St. 107, 111.

¹² See *Hamilton v. Glenn*, 85 Va. 901, 9 S. E. 129; *Hambleton v. Glenn*, 72 Md. 331, 20 Atl. 115; *McKim v. Glenn*, 66 Md. 479, 8 Atl. 130; *Morris v. Glenn*, 57 Ala. 628, 7 South. 90.

¹³ *Foreman v. Bigelow*, 4 Cliff. 508, Fed. Cas. No. 4,934; *Steacy v. Railroad Co.*, 5 Dill. 348, Fed. Cas. No. 13,329; 1 Cumming, Cas. Priv. Corp. 957; *ante*, p. 388.

¹⁴ 1 Mor. Priv. Corp. § 161; *Schenectady & S. Plank-Road Co. v. Thatcher*, 11 N. Y. 102, 108.

¹⁵ 1 Mor. Priv. Corp. § 161.

against the corporation, the transferror is not liable for assessments authorized to be made on "stockholders" beyond the amount of their shares.¹⁶

Right to Dividends.

It is a general rule, as shown in a preceding chapter, that dividends on shares belong to the person who is the owner of them at the time they are declared, without regard to the time during which the dividends were earned, or the time when such person acquired the shares.¹⁷ In the absence of a special agreement to the contrary, therefore, dividends declared before a transfer, though not payable until afterwards, belong to the transferror, and he may sue the corporation therefor after the transfer.¹⁸ But dividends declared after the transfer, though earned before, belong to the transferee.¹⁹ This rule may be changed by special agreement between the parties, and the agreement will be binding on the corporation if it has notice of it.²⁰ If it has not such notice, it may safely pay the dividends to the transferee.²¹

Statutory Liability of Stockholders.

As a rule, where by statute stockholders are made liable for the debts of the corporation, no liability attaches until the corporate property fails, and it becomes necessary to resort to the stockholders' liability, and such persons only as are then stockholders are subject to the liability. A valid and complete transfer of stock, therefore, in the absence of express provision to the contrary, relieves the transferror of all liability to creditors of the corporation, and the transferee becomes liable in his place. Such is the general rule; but there are some decisions to the contrary, and the peculiar provisions of particular statutes may require a different rule. The subject will be explained at length in treating of the rights and remedies of creditors.²²

¹⁶ Chouteau Spring Co. v. Harris, 20 Mo. 383.

¹⁷ Ante, p. 48.

¹⁸ Id.

¹⁹ Hyatt v. Allen, 56 N. Y. 553; Jones v. Railroad Co., 57 N. Y. 196; Jermain v. Railway Co., 91 N. Y. 483; March v. Railroad Co., 43 N. H. 515.

²⁰ 1 Mor. Priv. Corp. § 162.

²¹ Ante, p. 349.

²² Post, p. 578.

Pledgees, Trustees, etc., of Shares.

Persons to whom shares have been transferred as security for debts due them from the transferror, and who appear on the registration books of the corporation as owners of the shares, have the same rights as against the corporation, and are subject to the same liability to the corporation and to creditors, as if they owned the shares absolutely. And the same is true of trustees, or others in whose names the shares stand on the books, though they have no beneficial interest therein; at least if it does not appear that they hold as pledgees, trustees, etc. They are liable, for instance, to the corporation and to corporate creditors for an unpaid balance due on the shares.²³ They are also subject to the statutory liability of stockholders for debts of the corporation, and their liability is not limited to the extent of their interest.²⁴

LIEN OF CORPORATION ON SHARES.

156. At common law a corporation has no lien on the shares of its stockholders for debts due from them; but such a lien may be created by the charter, or by statute, or by a by-law, if there is express legislative authority therefor.

It is well settled that at common law a corporation has no lien on the shares of its stockholders for debts due to it from them.²⁵ The reason given is that a different rule would subvert the wholesome doctrine of the common law against secret liens.²⁶ It follows that the fact that a stockholder is indebted to the corporation does not of itself give the corporation any greater or different rights than any other creditors would have, and is no ground for a refusal of the corporation to recognize and register a bona fide transfer, unless a lien is given by the charter, or by statute, or by an authorized by-

²³ Pullman v. Upton, 96 U. S. 328, post, p. 583.

²⁴ Post, p. 583.

²⁵ Sargent v. Insurance Co., 8 Pick. (Mass.) 90; Massachusetts Iron Co. v. Hooper, 7 Cush. (Mass.) 183; Steamship Dock Co. v. Heron's Adm'r, 52 Pa. St. 280; Farmers' & Merchants' Bank v. Wasson, 48 Iowa, 336; Driscoll v. Manufacturing Co., 59 N. Y. 96, 102; Bank v. Lanier, 11 Wall. 369; Heart v. Bank, 2 Dev. Eq. (N. C.) 111; Dana v. Brown, 1 J. J. Marsh. (Ky.) 304.

²⁶ Driscoll v. Manufacturing Co., 59 N. Y. 96, 102.

law.²⁷ Whether, in the absence of charter or statutory authority, a corporation may by a by-law create a lien on its shares for debts due from its stockholders, is a question upon which the courts do not entirely agree. By the weight of authority, such a by-law is binding upon the stockholders, and upon transferees who are not bona fide purchasers; but it is ineffectual as against bona fide purchasers.²⁸

The legislature may, in the charter or by statute, give a corporation a lien on shares for debts due to it by its stockholders, or may give the corporation the power to create such a lien by a by-law. In such a case a lien attaches, and a transferee of the stock will take subject to it, whether he had notice or not; and the corporation may refuse to register the transfer until the indebtedness is paid.²⁹ A provision in the charter of a corporation that shares of stock shall be transferable only on the books of the corporation, according to rules established by it and all debts due and payable to the corporation by a stockholder must be satisfied before the transfer shall be made, gives the corporation a lien on shares for debts due by stockholders.³⁰ The lien given by statute to a corporation upon the shares of stockholders "indebted" to it, extends to all debts, whether payable presently or at a future time, except where the statute limits the lien to debts actually due and payable.³¹ Under the national banking act, a national bank cannot, by by-law or otherwise, acquire a lien upon the shares of its stockholders for debts due from them to the bank.³²

A corporation, which by its charter or otherwise is given a lien on its shares for debts due from its stockholders, may waive its rights in this respect; and, if it induces a purchaser of its shares to alter his condition in reliance upon its assurances that it has no adverse claim on the shares, it will be held to have waived any lien it may have had.³³

²⁷ See the cases cited above.

²⁸ Post, p. 457.

²⁹ *Union Bank v. Laird*, 2 Wheat. 390; *Brent v. Bank*, 10 Pet. 596; *Bishop v. Globe Co.*, 135 Mass. 132.

³⁰ *Union Bank v. Laird*, *supra*.

³¹ *Pittsburgh & C. R. Co. v. Clarke*, 29 Pa. St. 146, 151.

³² *Bullard v. Bank*, 18 Wall. 589.

³³ *National Bank v. Watontown Bank*, 105 U. S. 217. And see *Moore v. Bank*, 52 Mo. 377. The acts of an agent of the corporation relied upon as a waiver must have been within his authority or apparent authority. In *Bishop*

VALIDITY OF TRANSFERS.

157. A stockholder, unless restricted by the charter or by statute, may transfer his shares, and thereby cease to be liable as a stockholder, to any one who is capable of holding them, and assuming the liability of a stockholder. But, as against the corporation and its creditors,

- (a) He cannot transfer his shares colorably.**
- (b) In this country, he cannot transfer to a man of straw, or to an insolvent person, for the purpose of escaping liability. The rule is otherwise in England.**
- (c) He cannot transfer to a person who is incapable in law of assuming liability with respect to the shares, as**
 - (1) To an infant.**
 - (2) To an insane person.**
 - (3) To a married woman, where by the law of the particular jurisdiction she cannot assume liability.**
 - (4) To the corporation itself, or to another corporation, if it is incapable of purchasing and holding the shares.**

158. Shares are not transferable after dissolution of the corporation, so as to pass the legal title.

These questions are considered at length in a subsequent chapter in dealing with the liability of stockholders. It is the general rule that a stockholder, where there are no restrictions in the charter or in the statutes, has an absolute right to transfer his shares. This rule, however, is subject to exceptions. A transfer may be perfectly

v. Globe Co., 135 Mass. 132, it was held that a corporation was not estopped to assert its lien by the fact that, on the transferee's presenting the certificate for transfer, the person in charge of the transfer book promised to make the transfer and issue a new certificate as soon as a certain officer returned, it not appearing that such person had any authority, except to receive requests for transfers, and communicate them to the proper officers.

valid as between the parties themselves, and yet be invalid as against the corporation and creditors of the corporation. Thus, as we shall presently see, a stockholder cannot transfer his shares colorably to an insolvent or irresponsible person, and thereby escape liability as a stockholder to creditors of the corporation.³⁴ And, though in England the rule is different, in this country a stockholder cannot transfer to an insolvent person, when he knows that the corporation is insolvent, for the purpose of escaping his statutory liability, though the transaction is an out and out sale and transfer.³⁵ There is also an implied prohibition against a transfer of shares to an infant or any other person who is not capable in law of assuming the liabilities, as well as enjoying the rights, of the transferee in respect thereto.³⁶ So it is with transfers to the corporation, or to some other corporation, where it has no power to hold the shares.³⁷

Transfer after Dissolution.

The right of a stockholder in a corporation to sell and transfer his stock, and to pass the legal title of such stock to the purchaser, ceases upon the dissolution of the corporation. The interests of the several stockholders are then reduced to mere equitable rights to their several distributive shares of the funds of the corporation, upon principles of justice and equity among all the stockholders; and in making distribution each stockholder is to be charged with the debts due from him to the corporation, so as to equalize the distributive shares of all the stockholders in the fund after payment of all debts due by them respectively to the corporation. When a stockholder assigns his interest after dissolution of the corporation, the assignee takes subject to this rule.³⁸

MODE OF TRANSFER.

159. In the absence of express regulations by the legislature, or under legislative authority, shares of stock may be transferred, and the legal title vested in the transferee, by delivery of the certificate with a written assignment thereof, or with an assignment in blank indorsed thereon.

³⁴ Post, p. 582. ³⁵ Post, p. 582. ³⁶ Post, p. 581. ³⁷ Post, p. 581.

³⁸ James v. Woodruff, 10 Paige (N. Y.) 541, affirmed 2 Denio (N. Y.) 574.

160. The validity and completeness of a transfer depends upon the law of the state by which the corporation was created.

In the absence of a statutory or charter provision, or of a by-law passed in pursuance of legislative authority, prescribing an exclusive manner in which the stock of a corporation shall be transferred, the owner may transfer the same to a purchaser, pledgee, or donee by the delivery of the stock certificate, with a written assignment thereof. Such a transfer is sufficient at common law to convey the legal as well as the equitable title as against all persons, including the corporation.³⁹ The assignment may be in blank, and indorsed on the certificate, in which case the shares will pass from person to person by delivery of the certificate, without further indorsement; the person who may be the holder of the certificate having the right at any time to fill up the blank with his name.

What Law Governs.

The validity of a transfer of stock in a corporation, and its sufficiency to pass title to the transferee, depend upon the law of the state by which the corporation was created, and not upon the law of the state in which the transferor and transferee reside, and the transfer is made.⁴⁰

REGISTRATION OF TRANSFER.

161. It is generally provided by charter or statutory provisions, or by authorized by-laws, that shares shall be transferable only on the books of the corporation. In the absence of such a requirement no record is necessary. As to the effect of such a requirement, the authorities do not agree. The result of the cases may be thus stated:

(a) In some states it is held that until a transfer is registered, or deposited for registration, the

³⁹ *Boston Music-Hall Ass'n v. Cory*, 129 Mass. 435, 1 Cumming, Cas. Priv. Corp. 650; *McNeil v. Bank*, 46 N. Y. 325, 1 Cumming, Cas. Priv. Corp. 620. *W. D. Smith, Cas. Corp.* 71; *Scott v. Bank*, 15 Fed. 494, 1 Cumming, Cas. Priv. Corp. 687.

⁴⁰ *Black v. Zacharie*, 3 How. 483, 1 Cumming, Cas. Priv. Corp. 671.

legal title to the shares remains in the transferor, and the transferee has only an equitable title. Under this view, until registration,

- (1) The transferror remains the owner of the shares, as far as the acts and dealings of the corporation are concerned, unless it has notice of the transfer, in which case it must regard the equitable title of the transferee. In the absence of notice, it may hold the transferror liable as a stockholder, and may pay him dividends, and accord him other rights as the owner of the shares.
- (2) The corporation may, as far as it is concerned, waive registration.
- (3) Registration is not necessary to entitle a bona fide purchaser of shares from the holder of the legal title to prevail against equities of third persons.
- (4) Nor is it necessary to entitle an innocent purchaser from the apparent and registered owner, under an unauthorized assignment, to prevail against the true owner on the ground of estoppel.
- (5) Registration is necessary to relieve the transferror from the statutory liability to creditors of the corporation.
- (6) It is also necessary as against bona fide purchasers or pledgees from the transferror.
- (7) In most states, but not in all, attaching or execution creditors of the transferror after the transfer, but before registration, will prevail as against the transferee's equitable title, if they have levied in ignorance of the transfer; but, by the weight of authority, not if they had notice of it.

(8) In some jurisdictions it is held that failure to register a transfer, or deposit it for registration, is *prima facie* evidence of a secret trust, and, if unexplained, evidence of an intent to hinder and defraud creditors, so that, as to them, the transfer is void. Perhaps in some states it would be held that failure to deposit a transfer for registration is conclusive evidence of a secret trust.

(b) In some states it is held that the requirement of registration is intended solely for the benefit and protection of the corporation, and may be waived by it, and that it does not prevent an unregistered transfer from conveying, as against the transferror and all third persons, the whole title, legal as well as equitable.

162. Where a transfer is duly registered, issuance of a new certificate is not necessary to transfer the legal title.

No record is necessary to perfect the transfer of stock, unless it is required by statute, or by the charter or by-laws of the corporation.⁴¹ Almost all charters or acts of incorporation contain the provision that the stock shall be transferable on the books of the corporation in such manner as may be prescribed by the by-laws or articles of association. Often it is provided that they shall be transferable "only" on the books of the corporation. There is no difference in the meaning of these provisions.⁴² The cases are very far from being clear or in accord as to the effect of such a provision. On some points there is a direct conflict.

In some states the provision has been construed literally, and as excluding any other mode of transferring the legal title; and it is held in these states that until a transfer is registered, or at least deposited with the corporation for the purpose of registration, the le-

⁴¹ Sayles v. Bates, 15 R. I. 342, 5 Atl. 497.

⁴² See Williams v. Bank, 5 Blatchf. 59, Fed. Cas. No. 17,727.

gal title to the shares remains in the transferror, and the transferee has only an equitable title.⁴³

In other states it is held that such a provision is intended solely for the protection of the corporation, and can be waived or asserted at its pleasure. No effect is given to it except for the protection of the corporation, and it does not prevent a stockholder from parting with his interest by a mere assignment of his certificate, subject only to such liens as the corporation may have upon it,⁴⁴ and excepting the right of voting at stockholders' meetings, receiving dividends, etc. And it is held that, as between the parties themselves to a sale or pledge of shares, a delivery of the stock certificate, with an assignment and power of attorney to transfer the shares on the books of the corporation, passes the entire title, legal as well as equitable, in the shares, whether the transfer is registered or not.⁴⁵

By the weight of authority, unless authorized to do so by its charter or by some statute, a corporation could not pass by-laws restricting the power to transfer the title to stock to transfers on the books of the corporation.⁴⁶

Necessity as against the Corporation.

Even in those jurisdictions where an unregistered transfer is regarded as passing the legal title as between the parties, and, a fortiori, in those jurisdictions where it is held that the equitable title

⁴³ Fisher v. Bank, 5 Gray (Mass.) 373, 1 Cumming, Cas. Priv. Corp. 664; Colt v. Ives, 31 Conn. 25 (explaining the earlier Connecticut cases); Reed v. Copeland, 50 Conn. 488; Brown v. Adams, 5 Bliss. 181, Fed. Cas. No. 1,986; Black v. Zacharie, 3 How. 483, 1 Cumming, Cas. Priv. Corp. 671; Scott v. Bank, 15 Fed. 494, 1 Cumming, Cas. Priv. Corp. 687; Johnson v. Laffin, 5 Dill. 65, Fed. Cas. No. 7,393, 1 Cumming, Cas. Priv. Corp. 608. affirmed 103 U. S. 800; Union Bank v. Laird, 2 Wheat. 390; Sabin v. Bank, 21 Vt. 362; People's Bank v. Gridley, 91 Ill. 457; Becher v. Mill Co., 1 Fed. 276. And it has even been held that delivery of a certificate, properly indorsed, to the officers of the corporation, with a request to transfer the same, is not sufficient to pass the legal title. Brown v. Adams, supra.

⁴⁴ Ante, p. 413.

⁴⁵ McNeill v. Bank, 46 N. Y. 325, 1 Cumming, Cas. Priv. Corp. 620, W. D. Smith, Cas. Corp. 71; Isham v. Buckingham, 49 N. Y. 216; Duke v. Navigation Co., 10 Ala. 82; Mandlebaum v. Mining Co., 4 Mich. 465, 2 Cumming, Cas. Priv. Corp. 159; Baldwin v. Canfield, 26 Minn. 43, 1 N. W. 261. And see Blouin v. Hart, 80 La. Ann. 714.

⁴⁶ Sargent v. Railway Co., 9 Pick. (Mass.) 202; Driscoll v. Manufacturing Co., 59 N. Y. 96.

only passes, a transfer, until registered or deposited for registration, confers on the transferee, as between himself and the company, no right beyond that of having the transfer properly entered. Until that is done, the person in whose name the stock is registered is, as between himself and the company, the owner to all intents and purposes.⁴⁷ A transferee, for instance, until he has had his transfer registered, or deposited it for registration, has no right to vote at stockholders' meetings.⁴⁸ He also takes the risk, as against the corporation, of payment of the dividends to the person who appears as owner on the books of the corporation.⁴⁹ But, of course, he would be entitled to recover them from the person so receiving them in an action for money had and received to his use. Assets of a corporation, on dissolution, may, like dividends, be safely distributed to those who appear on its books as owners of stock, and the distribution will be valid as against persons claiming under an unregistered transfer, of which the corporation had no notice.⁵⁰ The unregistered transferee also takes the risk of any lien which the corporation may acquire on the shares for indebtedness of the registered holder.⁵¹ The transferror is not relieved from liability for calls, nor does the transferee become liable for calls, until the transfer is registered, when registration on the books is required.⁵²

In those jurisdictions where it is held that the provision is for the protection of the corporation, it may be waived by the corporation. Therefore, though a transferror may be held liable for calls made subsequently to the transfer, but before registration, he cannot be held liable where the corporation waives the requirement of registration expressly or by its mode of doing business, as by failing to keep a registry book.⁵³

⁴⁷ *People v. Robinson*, 64 Cal. 373, 1 Pac. 156.

⁴⁸ *People v. Robinson*, *supra*.

⁴⁹ *Ante*, p. 349.

⁵⁰ *Bank of Commerce's Appeal*, 73 Pa. St. 59.

⁵¹ *Union Bank v. Laird*, 2 Wheat. 390. See *Bank of Attica v. Manufacturers' & Traders' Bank*, 20 N. Y. 501.

⁵² *Marlborough Manuf'g Co. v. Smith*, 2 Conn. 579, 583.

⁵³ *Isham v. Buckingham*, 49 N. Y. 216. And see *American Nat. Bank v. Oriental Mills*, 17 R. I. 551, 23 Atl. 795; *Chemical Nat. Bank v. Colwell*, 132 N. Y. 250, 30 N. E. 644.

If a transfer is valid, the corporation is bound to register it. Any valid transfer in writing is valid as against the company, if, on being notified, it refuses to allow registration. A transferror, therefore, is not liable to the corporation for assessments authorized to be made on "stockholders" beyond their shares, after a valid assignment has been made, and the corporation has refused to register it.⁵⁴

Necessity as against Estoppel of Owner in Case of Unauthorized Transfer.

As we shall presently see, if the true owner of stock holds out another, or allows him to appear as having full power to dispose of the stock, and innocent third persons are thus led into dealing with the apparent owner, and taking a transfer from him, they will be protected, under the doctrine of equitable estoppel, against any claim by the true owner.⁵⁵ In such a case it is not necessary, as against the true owner, that their transfer shall have been registered.⁵⁶

Necessity as against Prior Equities of Third Persons.

The fact that a transfer by one who has the legal title to shares, and the apparent absolute power to dispose of the same, is not registered, does not affect the right of the transferee to prevail against prior equities of third persons. Thus a bona fide purchaser of certificates of stock, upon which a power of attorney, authorizing their transfer to any person, is indorsed by the person in whose name the certificates were issued, and who was the last registered holder of the shares, takes them relieved of a secret trust existing back of the registry, though his transfer is not registered.⁵⁷

Necessity as against Creditors of Corporation.

It is very generally held, even in those states where an unregistered transfer conveys the legal as well as the equitable title, that the statutory requirement of registration is intended for the protection of the creditors of the corporation, as well as of the corporation. And it is therefore held that a stockholder who has transferred his shares is not relieved from liability to creditors of the corporation until the trans-

⁵⁴ Chouteau Spring Co. v. Harris, 20 Mo. 383.

⁵⁵ Post, p. 431.

⁵⁶ Otis v. Gardner, 105 Ill. 436; and other cases cited post, p. 431.

⁵⁷ Winter v. Montgomery Gaslight Co., 89 Ala. 544, 7 South. 773, 2 Cumming, Cas. Priv. Corp. 163.

fer is registered. This question will be considered in a subsequent chapter.⁵⁸

Necessity as against Bona Fide Purchasers and Pledgees.

In those jurisdictions where it is held that an unregistered transfer does not convey the legal title, it is clear that an unregistered transferee cannot set up the transfer as against a bona fide purchaser or pledgee from the person who appears as owner on the books of the corporation. And even in those jurisdictions where it is held that an unregistered transfer passes the legal as well as the equitable title, as between the parties, the transferee will lose the shares by a fraudulent transfer on the books by the registered owner to a bona fide purchaser, though he may hold a certificate.⁵⁹ But in such a case the unregistered transferee will have a right of action against the corporation for allowing a transfer on the books in violation of his rights.⁶⁰

An unregistered transfer is not good as against subsequent bona fide purchasers of the stock at a sale on execution against the transferor, who appears on the books of the corporation as owner, where they have no notice of the transfer.⁶¹ It is otherwise if they have such notice.⁶²

By express provisions of the statute in some states, transfers of stock, if not registered within a certain time on the books of the corporation, are declared to be void as to bona fide creditors or purchasers without notice.

Necessity as against Creditors of Registered Owner.

In some of those states where an unregistered transfer does not convey the legal title it is held that an attachment or execution by a

⁵⁸ *Shellington v. Howland*, 53 N. Y. 371; *Dane v. Young*, 61 Me. 160; *McClaren v. Franciscus*, 43 Mo. 452; post, p. 580. But in *Laing v. Burley*, 101 Ill. 591, it was held that, where a corporation issues a certificate to a transferee of shares in lieu of the certificate issued to the prior owner, the transferee becomes a stockholder, and liable as such to creditors of the corporation, though the corporation fails to register the transfer as required by its by-laws.

⁵⁹ *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 80, 2 Cumming, Cas. Priv. Corp. 119, 137.

⁶⁰ *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 80, 2 Cumming, Cas. Priv. Corp. 119, 137.

⁶¹ *Naglee v. Wharf Co.*, 20 Cal. 529.

⁶² *Newberry v. Manufacturing Co.*, 17 Mich. 141.

creditor of the transferror and registered owner of shares will prevail against the transfer if it is not registered, or at least deposited for registration. These cases are based solely upon the ground that the legal title in such a case remains in the transferror, and is subject to attachment and execution for his debts, and does not rest on any idea of fraud, actual or constructive.⁶³ And it is further held that, as against the execution or attachment, it can make no difference that the corporation had notice of the transfer before the levy.⁶⁴ It has been held that, where registration is required, actual registration is necessary as against an execution or attaching creditor, and deposit for record is not sufficient.⁶⁵ But actual registration is not necessary if receipt for record be made sufficient to pass the title.⁶⁶

Even if an unregistered transfer be regarded as insufficient to pass the legal title, it passes an equitable title, and will be upheld as an equitable assignment. Therefore, by the weight of authority, an equitable assignment will prevail as against creditors of the transferror who attach the shares with full knowledge of the transfer.⁶⁷ It is otherwise if they have no notice of the transfer.⁶⁸ So the corporation itself, being a creditor of a stockholder, cannot, if it has notice of an equitable assignment of his shares, attach them before the transfer is registered, and so prevail as against the transferee, unless it is given a lien on shares for debts due from stockholders.⁶⁹

Some of the courts hold that, when shares are sold or pledged, there is no necessity to have the transfer registered on the books of the

⁶³ *Fisher v. Bank*, 5 Gray (Mass.) 373, 1 Cumming, Cas. Priv. Corp. 664; *Williams v. Bank*, 5 Blatchf. 59, Fed. Cas. No. 17,727; *People's Bank of Bloomington v. Gridley*, 91 Ill. 457; *Northrop v. Turnpike Co.*, 3 Conn. 544; *Oxford Turnpike Co. v. Bunnel*, 6 Conn. 552; *Skowhegan Bank v. Cutler*, 49 Me. 315. Compare *Sibley v. Bank*, 133 Mass. 515; *Colt v. Ives*, 31 Conn. 25.

⁶⁴ *Fisher v. Bank*, *supra*.

⁶⁵ *Northrop v. Turnpike Co.*, *supra*.

⁶⁶ *Oxford Turnpike Co. v. Bunnel*, *supra*.

⁶⁷ *Black v. Zacharie*, 3 How. 482, 1 Cumming, Cas. Priv. Corp. 671; *Scripture v. Soapstone Co.*, 50 N. H. 571, 1 Cumming, Cas. Priv. Corp. 677; *Buttrick v. Railroad Co.*, 62 N. H. 413; *Weston v. Mining Co.*, 6 Cal. 425; *State Ins. Co. v. Gennett*, 2 Tenn. Ch. 100; *State Ins. Co. v. Sax*, Id. 507; *Newberry v. Manufacturing Co.*, 17 Mich. 141.

⁶⁸ *Weston v. Mining Co.*, 5 Cal. 186; *State Ins. Co. v. Gennett*, *supra*; *State Ins. Co. v. Sax*, *supra*; *Buttrick v. Railroad Co.*, *supra*.

⁶⁹ *Scripture v. Soapstone Co.*, *supra*.

corporation, in order to make it good as against subsequent attaching creditors of the transferror, unless such a step is expressly required as against creditors by the charter of the corporation, or by some statute; and that, in the absence of a charter or statutory provision clearly showing an intention on the part of the legislature to make a transfer void as against creditors unless registered, a transfer as at common law will be sufficient.⁷⁰ In these states, therefore, in the absence of such an express statutory provision, there must be some element of fraud or estoppel to defeat the rights of an unregistered transferee, and to give the claims of creditors of the transferror priority.

Of course, in those jurisdictions where it is held that an unregistered transfer conveys the legal as well as the equitable title, the transfer will prevail as against an attaching creditor of the transferror, even though he has no notice of the transfer, unless there is some element of fraud or estoppel.

Where stock is held in trust by the registered holder, and the whole beneficial interest is in another, the stock does not pass to the registered holder's assignee in bankruptcy or insolvency.⁷¹

Same—Failure to Register as Evidence of Secret Trust.

Transfers of stock, if made with intent to hinder, delay, and defraud creditors, and not in good faith, are void as to creditors of the transferror to the same extent as a transfer of any other property with such intent would be. In some jurisdictions, retention of possession of property by the seller is evidence of a secret trust, and, if unexplained, the sale will be held fraudulent and void as to creditors

⁷⁰ *Broadway Bank v. McElrath*, 13 N. J. Eq. 24, 1 Cumming, Cas. Priv. Corp. 683; *Boston Music Hall Ass'n v. Cory*, 129 Mass. 435, 1 Cumming, Cas. Priv. Corp. 650; *Scott v. Bank*, 15 Fed. 494, 1 Cumming, Cas. Priv. Corp. 687. In *Broadway Bank v. McElrath*, supra, M. had delivered to the complainants certificates of stock in a corporation, accompanied by an assignment, and an irrevocable power of attorney for the transfer thereof, as security for certain debts. The charter of the corporation provided that its capital stock should be deemed personal property, and be transferable on the books of the corporation, and also that books of transfer of stock should be kept, and should be evidence of ownership of said stock in all elections and other matters submitted to the decision of the stockholders of the corporation. It was held that, notwithstanding such provisions, the transfer by M., though unregistered, was good as against an attachment subsequently levied by his creditor.

⁷¹ *Sibley v. Bank*, 133 Mass. 515.

of the seller. In other jurisdictions, retention of possession renders the sale, not merely *prima facie* fraudulent, but conclusively so. These doctrines as to the effect of retention of possession by the seller of property apply to sales of shares of stock. Unless there is such a change of possession as the nature of the property will permit, the sale, in some jurisdictions, will be conclusively fraudulent as to creditors; in others, *prima facie* so. The question therefore arises: What is a sufficient change of possession on a sale of shares? The supreme court of New Hampshire has held that, upon a sale or pledge of stock, there should be such a delivery as the nature of the thing allows; that, as against a subsequent attaching creditor, the transferee must be clothed with all the usual muniments and indicia of ownership; that the delivery will not be complete until an entry of the transfer is made upon the stock record, or notice is sent to the office of the corporation for that purpose; and that the omission to thus perfect the delivery will be *prima facie*, and if unexplained, conclusive, evidence of a secret trust, and therefore, as a matter of law, fraudulent and void as to the transferror's creditors.⁷²

If the failure to register a transfer of shares is explained, and the presumption of fraud rebutted, in those jurisdictions, at least, where it is rebuttable, the title of the transferee will prevail as against creditors of the transferror, even though they may attach the shares in ignorance of the transfer.⁷³ "The ground," said the Connecticut court,

⁷² *Pinkerton v. Railroad Co.*, 42 N. H. 424, 1 Cumming, Cas. Priv. Corp. 652. Where a transfer is made at a distance from the office of the corporation, and in another state, and the old certificates are surrendered, and new ones issued by the transfer agent of the corporation appointed for that purpose in such state, proof that the proper evidence of such transfer was sent to the keeper of the stock record, to be entered, by the earliest mail, although not received until an attachment was levied, will be a sufficient explanation of the want of delivery, and the transfer will be good as against the attaching creditor. *Pinkerton v. Railroad Co.*, *supra*. But where a pledge of stock was made in Boston by a transfer of the certificates to the pledgee, and nothing more was done for nearly a month, and then the old certificates were surrendered, and new ones issued by the transfer agent there, and notice given by the first mail to the office of the corporation in New Hampshire, it was held that the transfer was not good as against an attachment levied on the shares in New Hampshire before the issuance of the new certificates, and the notice to the office. *Pinkerton v. Railroad Co.*, *supra*.

⁷³ *Colt v. Ives*, 31 Conn. 25; *U. S. v. Vaughan*, 3 Bin. (Pa.) 394.

"on which stock sold, but not legally transferred (that is, on the books), is open to attachment by the creditors of the vendor, is the same upon which personal chattels sold but retained in the possession of the vendor are liable to attachment by the vendor's creditors. The principle in each case is, that the retention of possession is a badge of fraud; that is, is evidence of a fraudulent secret trust. * * * But it is well settled that this retention of possession in every case is only a badge; that is, is evidence of fraud, to be regarded as conclusive where the retention of possession is voluntary and unnecessary."⁷⁴

Issuance of New Certificate.

A transfer on the books of the corporation is sufficient to vest the title in the transferee, without the issuance of a new certificate in the name of the transferee.⁷⁵ The certificate, as we have seen, is merely evidence of title to shares, and is not at all necessary to constitute one a stockholder.⁷⁶

FORGED AND UNAUTHORIZED TRANSFERS.

163. Certificates of stock are not negotiable instruments, unless expressly made so by statute. Therefore a transferee under a forged assignment and power of attorney acquires no title as against the true owner. And the same is true of an unauthorized transfer by one who has stolen or found a certificate indorsed in blank by the true owner.

164. A transfer of certificates of stock by one who holds the legal title in trust, but who appears as absolute owner on the books of the corporation, conveys a good title, as against the cestui que trust, if the transferee is an innocent purchaser for value and without actual or constructive notice of the trust, but not otherwise.

⁷⁴ Colt v. Ives, supra.

⁷⁵ Chouteau Spring Co. v. Harris, 20 Mo. 383.

⁷⁶ Ante, p. 316.

165. If the owner of a certificate of stock allows another to appear as owner, with full power to dispose of it, and innocent third persons are thus led into dealing with the apparent owner, they will acquire title, as against him, by estoppel.
166. The doctrine of *lis pendens*, as constructive notice, does not apply to transfers of stock.

Certificates of shares of stock in a corporation are not negotiable instruments, like bills and notes, unless, as is the case in some jurisdictions, they are expressly made so by statute. And no mere usage among stockbrokers or others can make them so, for no usage is good if it conflicts with an established principle of law.⁷⁷ Certificates of stock are on the same footing as other nonnegotiable choses in action, and they are subject, therefore, to the general rule that an assignor can transfer no better title than he has himself.⁷⁸ It follows from this principle that, in the absence of negligence on the part of the owner of stock sufficient to operate as an estoppel against him, a transfer by a person who has no title to shares, and no authority from the owner to transfer the same, gives the transferee no title, as against the owner, though he may have purchased them in good faith for value, and without notice of the want of title or authority in the transferror. It is accordingly well settled that, in the absence of negligence, a forged indorsement and transfer of certificates of stock cannot divest the owner of his title, nor confer any rights, as against him, upon the transferee; and if the corporation recognizes the forged indorsement, and transfers the stock, so that the certificate is lost to the real owner, it may be compelled to replace it, or to pay him its value.⁷⁹ On the same principle, an innocent purchaser of a

⁷⁷ *East Birmingham Land Co. v. Dennis*, 85 Ala. 565, 5 South. 317, 1 Cumming, Cas. Priv. Corp. 647, W. D. Smith, Cas. Corp. 76.

⁷⁸ *East Birmingham Land Co. v. Dennis*, supra. And see *Sewall v. Power Co.*, 4 Allen (Mass.) 277, 282; *Shaw v. Spencer*, 100 Mass. 382; *Pollock v. Bank*, 7 N. Y. 274; *President, Directors & Co. of Mechanics' Bank v. New York & N. H. R. Co.*, 13 N. Y. 599; *Barstow v. Mining Co.*, 64 Cal. 388; *Hall v. Road Co.*, 70 Ill. 673; *Western Union Tel. Co. v. Davenport*, 97 U. S. 369, 1 Cumming, Cas. Priv. Corp. 643.

⁷⁹ *Western Union Tel. Co. v. Davenport*, 97 U. S. 369, 1 Cumming, Cas. Priv. Corp. 643; *Hildyard v. South-Sea Co.*, 2 P. Wms. 76; *Sewall v. Power Co.*, 4

certificate of stock indorsed in blank by the owner, and stolen from him, or lost by him, without negligence on his part, acquires no title, as against the owner.⁸⁰ "Neither the absence of blame on the part of the officers of the company in allowing an unauthorized transfer of stock, nor the good faith of the purchaser of stolen property, will avail as an answer to the demand of the true owner. The great principle that no one can be deprived of his property without his assent, except by the processes of the law, requires, in the cases mentioned, that the property wrongfully transferred or stolen should be restored to its rightful owner."⁸¹

One who is entitled to stock, certificates for which have been wrongfully transferred to another, may maintain a bill in equity to have the wrongful certificates canceled, and certificates issued to himself, if the loss of the stock cannot be adequately compensated in a common-law action.⁸²

Liability of Transferee.

A corporation may maintain an action for damages against a person who presents a forged or unauthorized power of attorney to transfer stock, upon the faith of which the corporation transfers the stock and suffers loss, though such person acted in good faith.⁸³

Transfers by Trustees.

Where the person who appears on the books of the corporations as the absolute owner of stock holds the stock in trust, a purchaser and transferee from him, if he has actual or constructive notice of the trust, takes subject to the equitable rights of the cestui que trust. And, if the certificate shows on its face that it is held in trust, transferees are charged with notice of the trust, and with the duty of inquiring into the authority of the holder to transfer the same.⁸⁴ The rule

Allen (Mass.) 277; Pratt v. Manufacturing Co., 123 Mass. 110; Pollock v. Bank, 7 N. Y. 274; Machinists' Nat. Bank v. Field, 126 Mass. 345, 2 Cumming, Cas. Priv. Corp. 175. And see Taft v. Railroad Co., 84 Cal. 131, 24 Pac. 436.

⁸⁰ East Birmingham Land Co. v. Dennis, 85 Ala. 565, 5 South. 317, 1 Cumming, Cas. Priv. Corp. 647, W. D. Smith Cas. Corp. 76; Knox v. Eden Musee American Co., 148 N. Y. 441, 42 N. E. 988; Barstow v. Mining Co., 64 Cal. 388, 1 Pac. 349; Sherwood v. Mining Co., 50 Cal. 412.

⁸¹ Western Union Tel. Co. v. Davenport, *supra*.

⁸² Walker v. Railway Co., 47 Mich. 338, 11 N. W. 187. See post, p. 435.

⁸³ Boston & A. R. Co. v. Richardson, 135 Mass. 473.

⁸⁴ Shaw v. Spencer, 100 Mass. 382. But see Albert v. Bank, 1 Md. Ch. 407.

is different where the transferee of a certificate has no notice that it is held in trust, and there is nothing to put him on inquiry. It is a general rule that when the legal title to property, and the apparent unlimited power of disposition, are vested in a person, the rights of a purchaser from him for a valuable consideration, without notice of a secret trust upon which the property is held, are unaffected. The purchaser in such a case acquires an equity equal to the outstanding equity of which he has no notice, and this, coupled with the legal title, prevails against the prior equity. This principle is applicable to transfers of certificates of stock. If a person who holds the legal title to certificates in trust appears on the books of the corporation as the absolute owner, a purchaser and transferee of the certificates for value, and without actual or constructive notice of the trust, acquires a good title, as against the cestui que trust. And this is true whether his transfer has been registered on the books of the corporation or not.⁸⁵ This applies to transfers by executors. In the case of executors, however, purchasers of stock from them, knowing their character, are chargeable with notice of the contents of the will.⁸⁶ At common law, executors have the same power over the disposition of the testator's personal property as the testator himself would have, except in so far as there may be restrictions in the will; and, where such is the case, he has power to sell stock belonging to the estate, and innocent purchasers will acquire title, though he may be selling the same to convert it to his own use.⁸⁷ If his powers are restricted by statute, as is now generally the case, a sale of stock must be made in compliance with the statute, or no title will pass. Thus, if an executor sells stock belonging to the estate at a private sale, without an application to the court, when a statute authorizes a sale at public auction only, unless an order of court is obtained authorizing a private sale, the sale passes no title to the stock, though the transfer is entered on the books of the corporation.⁸⁸

⁸⁵ *Winter v. Gaslight Co.*, 89 Ala. 544, 7 South. 773, 2 Cumming, Cas. Priv. Corp. 163. And see *Weyer v. Bank*, 57 Ind. 198; *Albert v. Bank*, 1 Md. Ch. 407; *Lowry v. Bank, Taney*, 310, Fed. Cas. No. 8,581.

⁸⁶ See *Lowry v. Bank, Taney*, 310, Fed. Cas. No. 8,581.

⁸⁷ *Lowry v. Bank*, *supra*; *Weyer v. Bank*, 57 Ind. 198.

⁸⁸ *Weyer v. Bank*, *supra*.

Estoppel of True Owner in Case of Unauthorized Transfer.

Certificates of stock and unauthorized transfers are subject to the doctrine of equitable estoppel. According to this doctrine, if the true owner of certificates of stock holds out another, or allows him to appear, as having full power of disposition thereof, and innocent third persons are thus led into dealing with the apparent owner, they will be protected, as against any claim by the true owner.⁹⁰ Their rights in such cases do not depend upon the actual title or authority of the party with whom they deal directly, but are based upon the conduct of the real owner, which precludes him from disputing, as against them, the existence of the title or authority which, through negligence or mistaken confidence, he caused or allowed to appear to be vested in the party making the transfer.⁹¹ In *McNeil v. Tenth Nat. Bank*,⁹¹ the owner of shares in a corporation delivered to his brokers, to secure a balance of account, the certificates of the shares, indorsed with a blank assignment and irrevocable power to transfer the same on the books of the corporation, signed and sealed by himself, and expressed to be "for value received"; and the brokers, without his knowledge or consent, pledged the shares, for their own indebtedness, to one who had no actual knowledge of the title under which they held. It was held that the pledgee of the brokers acquired a good title to the shares, as against the owner, who was estopped to deny the apparent title of the brokers under his indorsement and irrevocable power of attorney.

This doctrine applies only on the ground that the owner of the stock allows the holder of the certificate to appear as owner. It does not apply, therefore, where the holder of the certificate, in transferring it without authority, does not pretend to own the stock and to act for himself, but claims to act for the owner, and under authority from him. In such a case the owner would not be estopped unless he held the transferror out as having the particular authority claimed.

⁹⁰ *McNeil v. Bank*, 46 N. Y. 325, 1 Cumming, Cas. Priv. Corp. 620, W. D. Smith, Cas. Corp. 71; *Cherry v. Frost*, 7 Lea (Tenn.) 1; *Jarvis v. Rogers*, 13 Mass. 105; *Colonial Bank v. Cady*, 15 App. Cas. 267, 1 Cumming, Cas. Priv. Corp. 629; *Otis v. Gardner*, 105 Ill. 438; *Mt. Holly Lumberton & Medford Turnpike Co. v. Fenece*, 17 N. J. Eq. 117; *Prall v. Tilt*, 28 N. J. Eq. 479; *Walker v. Railway Co.*, 47 Mich. 338, 11 N. W. 187; *Burton's Appeal*, 93 Pa. St. 214.

⁹¹ *McNeil v. Bank*, supra.

⁹¹ Supra.

In *Merchants' Bank of Canada v. Livingston*,⁹² a pledgee of a certificate of stock which was indorsed by the owner in blank, with an irrevocable power of attorney to transfer the same on the books of the corporation, applied to the plaintiff for a loan, offering the stock as security. He did not claim to own the stock, nor ask the loan on his own account, but stated that he wanted it for his client. The plaintiff, in good faith, made the loan, and took the certificate as security, and contended that the owner was estopped, under the doctrine of *McNeil v. Tenth Nat. Bank*. It was held that there was no estoppel, as the owner had not held the pledgee out as having authority to borrow money for him and pledge the stock as security, though he would have been estopped if the pledgee had sold or pledged the stock as his own, as he was clothed with apparent ownership.

Simply intrusting the possession of a certificate of stock to another as depositary, pledgee, or other bailee, or even under a conditional, executory contract of sale, will not preclude the owner from asserting his title in case of an unauthorized disposition of it by the person so intrusted; for the mere possession of chattels, by whatever means acquired, if there is no other evidence of property or authority to sell from the true owner, will not enable the possessor to give a good title.⁹³

If an indorsement of assignment and power of attorney on a certificate of stock is sufficient to put persons dealing with the holder upon inquiry as to his title, or if it may mean on its face either an absolute transfer, or a transfer for a particular purpose only, persons who take the stock from the holder are chargeable with notice of his title, and the owner will not be estopped, as against them, to deny that the transfer was absolute. This principle was applied in *Colonial Bank v. Cady*,⁹⁴ where the executors of the former owner of shares indorsed the certificates with an assignment and power of attorney in blank, and sent them to a broker for the purpose of having them registered in their names as executors. The broker fraudulently deposited the certificates with a bank as security for advances. It was held that the bank acquired no title to the stock, as against the executors, though it took the certificates in perfect good faith, and without ac-

⁹² 74 N. Y. 223; 2 Cumming, Cas. Priv. Corp. 142.

⁹³ *McNeil v. Bank*, *supra*.

⁹⁴ 15 App. Cas. 267, 1 Cumming, Cas. Priv. Corp. 620.

tual notice of the character in which the broker held them, and for these two reasons: In the first place, certificates so indorsed by executors were not treated on the stock exchange as being in order, or received as sufficient security for advances, unless duly authenticated, and this was sufficient to put the bank upon inquiry. In the second place, the conduct of the executors in delivering the transfers indorsed by them as executors was consistent either with an intention to sell or pledge the shares, or with an intention merely to have themselves registered as the owners, and therefore they were not estopped to assert that they did not intend an absolute transfer.

Effect of Judicial Proceedings.

The question how far a purchaser of stock, where a certificate therefor is outstanding, is affected by previous or pending judicial proceedings concerning the ownership of the stock, is not altogether clear. It has been held in New York that the doctrine of *lis pendens* does not apply to a sale of shares of stock, and, therefore, that the pendency of an action concerning the title to shares, the certificate of which is outstanding, is not constructive notice to one who purchases the certificate, and that a judgment rendered after the transfer does not defeat his title.⁹⁵ It was held by Judge Woodruff, in the circuit court of the United States for the Southern district of New York, that a decree of a court having jurisdiction of the subject-matter and of the parties, vesting the title to stock in a person other than the holder of the outstanding certificate, and a transfer made by a master in pursuance thereof, and made known to the corporation, is a complete protection to the corporation against purchasers of the outstanding certificate, though they pay value and have no notice of the decree.⁹⁶ Such a decree and transfer could not affect the title of one who purchased the outstanding certificate before commencement of the action, nor, if the New York cases are sound, after the commencement

⁹⁵ *Holbrook v. Zinc Co.*, 57 N. Y. 616, 2 Cumming, Cas. Priv. Corp. 152. Compare *Leitch v. Wells*, 48 N. Y. 585. The pendency of an action in another state concerning the title to stock would not be notice to a purchaser of the outstanding certificate, even if the doctrine of *lis pendens* were applicable to a sale of shares. *Holbrook v. Zinc Co.*, *supra*.

⁹⁶ *Sprague v. Manufacturing Co.*, 10 Blatchf. 173, Fed. Cas. No. 13,249, 1 Cumming, Cas. Priv. Corp. 661.

of the action, but before the decree.⁹⁷ And the later cases tend to hold that a purchaser of outstanding certificates, without notice, even after a decree in a suit to which he was not a party, declaring them void and canceling them, would not be affected by the decree, but could hold the corporation liable.⁹⁸

LIABILITY OF INDORSER OF FORGED CERTIFICATE

167. Though there is authority to the contrary, by the better opinion one who indorses a certificate of stock in blank thereby warrants its genuineness, and will be liable to subsequent bona fide purchasers.

It has been held that the signing of a transfer in blank on a certificate of stock is a warranty of the genuineness of the certificate, and that a transferror, therefore, who indorses a forged certificate in blank, though he may have taken the same in good faith, and may be ignorant of the forgery, is liable to subsequent bona fide purchasers. In *Matthews v. Massachusetts Nat. Bank*,⁹⁹ a stock certificate originally for 2 shares of stock in the name of one Coe, which had been fraudulently altered so as to purport to be for 200 shares in the name of the defendant as collateral, was received in good faith by the defendant from Coe as collateral security for a loan from him. On payment of the loan by Coe the defendant signed a transfer in blank upon the back of the certificate, and delivered it to Coe. Afterwards the plaintiff, in good faith, received the same certificate from Coe as collateral security for a loan then made to him. The plaintiff's debt was not paid by Coe, and, the certificate proving worthless, the plaintiff sued the defendant for damages, on the ground that the defendant, by its indorsement, warranted the certificate to be genuine. It was held that he could recover.

⁹⁷ *Holbrook v. Zinc Co.*, *supra*; *Joslyn v. Distilling Co.*, 44 Minn. 183, 46 N. W. 337, 2 Cumming, Cas. Priv. Corp. 177; *Bean v. Trust Co.*, 122 N. Y. 622, 26 N. E. 11, 2 Cumming, Cas. Priv. Corp. 179.

⁹⁸ Cases cited in the preceding note. See post, p. 442.

⁹⁹ *Holmes*, 396, Fed. Cas. No. 9,286.

LIABILITY OF CORPORATION ARISING FROM UNAUTHORIZED OR INVALID TRANSFER.

168. A corporation is liable to the owner of stock if it registers a forged or unauthorized or invalid transfer, unless the owner is estopped by negligence.

169. If the holder of the legal title to a certificate of stock appears to be the absolute owner, and the corporation has no notice that the fact is otherwise, it will incur no liability to the equitable owner by recognizing a transfer from the holder.

As we have just seen, in the absence of elements of estoppel a forged or unauthorized indorsement or transfer of certificates of stock cannot divest the owner of his title, nor confer any rights, as against him, upon the transferee. If, therefore, a corporation recognizes a forged or unauthorized indorsement and transfer, and transfers the stock and issues a new certificate, so that the certificate is lost to the real owner, it may be compelled to replace it, or pay him its value. And it can make no difference whatever that the corporation has not been guilty of fraud or negligence.¹⁰⁰ No liability, however, will attach to the corporation where the owner of the stock has been negligent. In such a case he will be estopped to deny the title of the transferee, and this estoppel will inure to the benefit of the corporation.¹⁰¹

Not only does a corporation, in permitting a transfer of stock to be made under a power of attorney, take the risk of the power of attorney being genuine and not a forgery, and of its being authorized, but it also takes the risk of its validity in other respects; and it will be liable if it was void because executed by a married woman, or if it was executed by an infant or insane person, and has been avoided. And it makes no difference that the corporation was not guilty of actual fault.¹⁰² The corporation has ample means to protect itself,

¹⁰⁰ *Telegraph Co. v. Davenport*, 97 U. S. 369, 1 Cumming, Cas. Priv. Corp. 643; *Taft v. Railroad Co.*, 84 Cal. 131, 24 Pac. 436. See ante, p. 428, where the cases are collected.

¹⁰¹ Ante, p. 431.

¹⁰² *Chew v. Bank*, 14 Md. 299.

for it may refuse to recognize a power of attorney until satisfied of its genuineness and validity, and may require the personal attendance of the party for the purpose of determining such questions of fact as may give rise to disputes.¹⁰³

If the holder of a certificate of stock appears to be the absolute owner, and the corporation has no notice that the fact is otherwise, it may safely issue a new certificate to his transferee, which, if taken in good faith and for value, will vest a perfect title in him; and in such a case no liability attaches to the corporation, in favor of an equitable owner of the shares, for permitting the transfer and issuing the new certificate.¹⁰⁴ But, for the protection of the equitable owner of shares, the corporation is bound to use reasonable care in recognizing transfers and issuing new certificates; and if, by the form of the certificate or otherwise, the corporation has notice that the transferror is not the absolute owner, but holds the shares by such a title that he may not have authority to transfer them, the corporation is not obliged, without evidence of such authority, to issue a certificate to his assignee; and if, without making any inquiry, it does issue a new certificate, and the equitable owner is injured thereby, he may hold the corporation liable, and this without proof of fraud or collusion. All the authorities agree that the corporation is liable where it has notice that the transferror holds the stock in trust, and issues a new certificate without inquiry as to whether the transfer is authorized.¹⁰⁵

In case of transfers by an executor, the corporation is chargeable with notice of the will and its contents. But, since an executor has authority to sell stock to pay debts of the testator, the corporation does not render itself liable by registering a transfer by him, if it has no reasonable ground for supposing that he is misapplying the assets, though the stock may be specifically bequeathed.¹⁰⁶ If, however, it has reasonable grounds for supposing the executor is misapplying the assets, and permits a transfer, it will be liable.¹⁰⁷

¹⁰³ Chew v. Bank, *supra*.

¹⁰⁴ Loring v. Salisbury Mills, 125 Mass. 150.

¹⁰⁵ Loring v. Salisbury Mills, *supra*; Shaw v. Spencer, 100 Mass. 382.

¹⁰⁶ Lowry v. Bank, Taney, 310, Fed. Cas. No. 8,581.

¹⁰⁷ Lowry v. Bank, *supra*.

LIABILITY OF CORPORATION ON CERTIFICATES ISSUED FRAUDULENTLY, WITHOUT AUTHORITY, ETC.

- 170. If the officers of a corporation, having apparent authority to issue certificates, issue certificates fraudulently, or without actual authority, or by mistake, to persons not entitled thereto, it will be liable to bona fide purchasers and transferees thereof.**
- 171. If a corporation registers a transfer and issues a new certificate without surrender of the outstanding certificate, it will be liable on both certificates to bona fide purchasers and transferees thereof.**

A corporation, by issuing a certificate of stock affirming that the person designated therein is the owner of a certain number of shares, transferable in the manner indicated thereon, becomes estopped, as against bona fide purchasers of the certificate, to say that it was issued without authority, or to a person not entitled. Therefore, if a corporation recognizes a forged or unauthorized transfer, and registers the same in the name of the transferee, and issues a new certificate to him, it will be liable to bona fide purchasers from the transferee, unless there is some element of estoppel, as against the real owner, which will prevent him from denying the transferee's title. It is not necessary that the corporation shall have been guilty of fraud or negligence. By thus holding the transferee out as the owner of stock, it is estopped to deny his title, as against bona fide purchasers.¹⁰⁸

Such a transfer cannot affect the title of the real owner, where there is no element of estoppel against him, and therefore it cannot substitute the purchaser as a stockholder in his stead.¹⁰⁹ If the corporation had power to issue new shares, the certificate issued to the transferee will be valid, and will make the holder a stockholder. If

¹⁰⁸ *Mandlebaum v. Mining Co.*, 4 Mich. 465, 2 Cumming, Cas. Priv. Corp. 159; *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 2 Cumming, Cas. Priv. Corp. 119; *Simm v. Telegraph Co.*, 5 Q. B. Div. 188, 2 Cumming, Cas. Priv. Corp. 165; *Machinists' Nat. Bank v. Field*, 126 Mass. 345, 2 Cumming, Cas. Priv. Corp. 175.

¹⁰⁹ See dictum in *Moore v. Bank*, 111 U. S. 156, 4 Sup. Ct. 345, 2 Cumming, Cas. Priv. Corp. 144.

it had already issued the full amount of stock authorized by its charter, the certificate cannot confer rights of membership, for an increase of stock would be ultra vires and void; and the remedy of a purchaser is by action against the corporation for damages, in which he may recover the value of the stock.¹¹⁰

It has been held that by registering a forged or unauthorized transfer, and issuing a new certificate to the transferee, the corporation is estopped to deny the validity of the transfer, even as against the transferee himself;¹¹¹ but by the better opinion the estoppel does not operate in favor of the transferee, for he has not taken the certificate on the faith of the corporation's conduct in issuing it and recognizing the transfer as valid, but on the faith of the forged or unauthorized assignment and power of attorney.¹¹² And the corporation in such a case may maintain an action against him for the damages it may have sustained.¹¹³ Nor does a corporation, by registering a forged or unauthorized transfer and issuing a new certificate, become liable to one who takes the certificate with notice of the forgery or want of authority, or of facts sufficient to put him upon inquiry.¹¹⁴

If an officer of a corporation, whose duty or apparent duty it is to issue certificates of stock, issues spurious certificates to himself or to another, the corporation will be liable to bona fide purchasers or pledgees of the certificates for the damages sustained by them.¹¹⁵

¹¹⁰ See the cases cited in note 108, supra.

¹¹¹ *Ashby v. Blackwell*, 2 Eden, 299; decision of Lindley, J., in *Simm v. Telegraph Co.*, 5 Q. B. Div. 188, 2 Cumming, Cas. Priv. Corp. 165.

¹¹² Decision of court of appeal in *Simm v. Telegraph Co.*, 5 Q. B. Div. 188, 2 Cumming, Cas. Priv. Corp. 165; *Hildyard v. South-Sea Co.*, 2 P. Wms. 76; *Boston & A. R. Co. v. Richardson*, 135 Mass. 473. See *Hall v. Road Co.*, 70 Ill. 673.

¹¹³ *Boston & A. R. Co. v. Richardson*, 135 Mass. 473.

¹¹⁴ See *Moore v. Bank*, 111 U. S. 156, 4 Sup. Ct. 345, 2 Cumming, Cas. Priv. Corp. 144.

¹¹⁵ *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 2 Cumming, Cas. Priv. Corp. 119; *Titus v. President, etc.*, 61 N. Y. 237; *Tome v. Railroad Co.*, 39 Md. 36, 17 Am. Rep. 540; *Fifth Ave. Bank v. Forty-Second St. & G. St. Ferry R. Co.*, 137 N. Y. 231, 33 N. E. 378, 2 Cumming, Cas. Priv. Corp. 149; *Bank of Batavia v. New York, L. E. & W. R. Co.*, 106 N. Y. 199, 12 N. E. 433; *Manhattan Beach Co. v. Harned*, 27 Fed. 484; *Shaw v. Mining Co.*, 13 Q. B. Div. 103; *Allen v. Railroad Co.*, 150 Mass. 200, 22 N. E. 917; *Farrington v. Railroad Co.*, 150 Mass. 406, 23 N. E. 109; post, p. 525, note 347.

There will be no liability, however, to persons who take the certificates with notice of their invalidity, or with knowledge of facts sufficient to put them on inquiry.¹¹⁶ If the corporation had authority under its charter to issue additional shares of stock, such certificates will be binding, and will make the purchasers stockholders. If, however, the full amount of stock authorized by the charter had already been issued, the certificates will be void, and the purchaser's only remedy against the corporation is an action for damages.¹¹⁷

No liability will attach to a corporation, in the absence of negligence, on account of certificates fraudulently issued by an officer, if the issuance of them had no relation whatever to the authority conferred upon him.¹¹⁸

A stock certificate issued by a corporation having power to issue the same, in which it is stated that a designated person is the owner of a certain number of shares of stock transferable on the books of the corporation, on the indorsement and surrender of the certificate, is a continuing affirmation as to the ownership of the stock, and that the corporation will not transfer the stock upon its books unless the certificate is first surrendered. It is an assurance to the commercial world that the shares of stock are the property of the person designated, and that he has the power and right to transfer and sell the

¹¹⁶ *Moore v. Bank*, 111 U. S. 156, 4 Sup. Ct. 345, 2 Cumming, Cas. Priv. Corp. 144. In this case the plaintiff lent money to the cashier of the defendant bank on his representation that he owned stock in the bank which he would transfer to her as collateral to secure the loan. He fraudulently signed and issued a certificate directly to her, using blank certificates which had been signed by the president, and left with him to be used if needed, and marked the stub in the certificate book so as to show that the blank had been destroyed. The certificate showed on its face that stock was transferable only on the books of the bank, and on surrender of the original certificate. Of course, the plaintiff never saw any original certificate, and no certificate was or could have been surrendered, and there was no evidence that the bank had ever ratified the transaction, or received any benefit from it. It was held that the plaintiff could not hold the bank liable. And see *Farrington v. Railroad Co.*, 150 Mass. 406, 23 N. E. 109; *Hill v. Publishing Co.*, 154 Mass. 172, 28 N. E. 142. Compare *Allen v. Railroad Co.*, 150 Mass. 200, 22 N. E. 917; *Shaw v. Mining Co.*, 13 Q. B. Div. 103.

¹¹⁷ See the cases above cited.

¹¹⁸ Post, p. 526, and cases there referred to.

stock, until this power and right has been lawfully terminated.¹¹⁹ It is therefore not only the right, but the duty, of a corporation not to register a transfer on its books and issue a new certificate to the transferee without production and surrender of the original certificate. This is generally expressly required by the terms of certificates, or by the charter or by-laws of the corporation, but the duty is the same where there is no such express requirement.¹²⁰ If a corporation does register a transfer and issue a new certificate without surrender of the outstanding certificate, a bona fide purchaser of the new certificate may hold it liable thereon. If the corporation had the power to increase its stock, he will be entitled to shares. If it had no such power, the purchaser may maintain an action for damages. Purchasers of the outstanding certificates in such cases have a right to assume that no transfer has been made by the corporation, and cannot be affected by a transfer on its books of which they had no notice.¹²¹ If the corporation refuses to recognize them as stockholders by reason of their ownership of the outstanding certificate, they may maintain an action against it for damages, and recover the value of the stock.¹²²

REMEDY AGAINST CORPORATION FOR REFUSAL TO RECOGNIZE TRANSFER.

172. If a corporation, without legal ground, refuses to recognize and register a transfer, the transferee may sue in equity to compel it to do so, or may sue at law to recover the value of the stock. Some of the courts hold that mandamus is not a proper remedy, but it is allowed in some states.

¹¹⁹ *Joslyn v. Distilling Co.*, 44 Minn. 183, 46 N. W. 337, 2 Cumming, Cas. Priv. Corp. 177.

¹²⁰ 1 Cook, Stock, Stockh. & Corp. Law, §§ 358-360.

¹²¹ See *Hall v. Road Co.*, 70 Ill. 673.

¹²² *First Nat. Bank v. Lanier*, 11 Wall. 369; *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 2 Cumming, Cas. Priv. Corp. 119; *Holbrook v. Zinc Co.*, 57 N. Y. 616, 2 Cumming, Cas. Priv. Corp. 152; *Bean v. Trust Co.*, 122 N. Y. 622, 26 N. E. 11, 2 Cumming, Cas. Priv. Corp. 179; *Joslyn v. Distilling Co.*, 44 Minn. 183, 46 N. W. 337, 2 Cumming, Cas. Priv. Corp. 177.

If a corporation whose shares of stock are transferable only on its books refuses to register a transfer, without legal ground for such refusal, a court of equity may compel it to register the transfer, in a suit brought by the transferee for that purpose.¹²³ Or the transferee may maintain an action at law to recover damages for such refusal, and recover the value of the stock. He may maintain an action *ex delicto*, or he may maintain *assumpsit*, for the law implies a promise by the corporation to perform the duty which it owes to transferees of shares.¹²⁴

Some of the courts have held that *mandamus* is not a proper remedy to compel a corporation to recognize a person as a member, or to register transfers.¹²⁵ It has been allowed, however, in some states.¹²⁶

The mere fact that the purchaser of shares is a rival of the corporation in business, and has been engaged in competition and in litigation with it, and is hostile to it, is no ground for the refusal of a court of equity to compel the corporation to register his transfer.¹²⁷

COMPELLING CORPORATION TO ISSUE NEW CERTIFICATES.

173. A corporation, not having been guilty of fraud or wrong, cannot be compelled to issue new certificates of stock while the old certificates are outstanding, unless the decree protects it against liability on the outstanding certificates.

¹²³ *Mechanics' Bank v. Seton*, 1 Pet. 200; *Rice v. Rockefeller*, 134 N. Y. 174, 81 N. E. 907, 2 Cumming, Cas. Priv. Corp. 181. *Walker v. Detroit Transit Ry. Co.*, 47 Mich. 338, 11 N. W. 187.

¹²⁴ *Ang. & A. Corp.* § 381; *Kortright v. Bank*, 20 Wend. (N. Y.) 91; *Morgan v. Bank*, 8 Serg. & R. (Pa.) 73; *Sargent v. Insurance Co.*, 8 Pick. (Mass.) 90; *Case v. Bank*, 100 U. S. 446; *Pinkerton v. Railroad Co.*, 42 N. H. 424, 1 Cumming, Cas. Priv. Corp. 652; *Scripture v. Soapstone Co.*, 50 N. H. 571, 1 Cumming, Cas. Priv. Corp. 677.

¹²⁵ *Lamphere v. Lodge*, 47 Mich. 429, 11 N. W. 268.

¹²⁶ *Green Mount & S. L. T. Co. v. Bulla*, 45 Ind. 1; *State v. McIver*, 2 S. C. 25; *People v. Crockett*, 9 Cal. 112; *In re Klaus*, 67 Wis. 401, 29 N. W. 582.

¹²⁷ *Rice v. Rockefeller*, 134 N. Y. 174, 81 N. E. 907, 2 Cumming, Cas. Priv. Corp. 181.

Since a certificate of stock is a continuing affirmation by the corporation that the person designated is the owner of the stock, and has the right to transfer the same, so long as the certificate is outstanding, and it will be liable to bona fide purchasers of the certificate, it follows that the court cannot compel it to issue a new certificate on the ground that the old certificate was issued to the wrong person (there having been no fraud on the part of the corporation), so long as the old certificate is outstanding, unless by the decree it protects the corporation against liability on the outstanding certificate.¹²⁸ The corporation would be liable to bona fide purchasers of the outstanding certificate even pending a suit to cancel the same and to compel the issuance of the new certificate, for the doctrine of *lis pendens*, as we have seen, does not apply to the sale and transfer of shares of stock.¹²⁹ The later cases seem to show that not even a decree of the court declaring an outstanding certificate void, and canceling the same, would relieve the corporation from liability to bona fide purchasers of the outstanding certificate without notice of the suit or the decree.¹³⁰

¹²⁸ *Joslyn v. Distilling Co.*, 44 Minn. 183, 46 N. W. 337, 2 Cumming, Cas. Priv. Corp. 177; *Bean v. Trust Co.*, 122 N. Y. 622, 26 N. E. 11, 2 Cumming, Cas. Priv. Corp. 179.

¹²⁹ *Holbrook v. Zinc Co.*, 57 N. Y. 616, 2 Cumming, Cas. Priv. Corp. 152.

¹³⁰ See the cases cited in note 97, *supra*. But see, *contra*, *Sprague v. Manufacturing Co.*, Fed. Cas. No. 13,249, 1 Cumming, Cas. Priv. Corp. 661.

CHAPTER XIII.

MANAGEMENT OF CORPORATIONS—OFFICERS AND AGENTS.

- 174-177. Powers of the Majority of Stockholders.
- 178-181. By-Laws.
- 182-184. Stockholders' Meetings.
- 185-188. Voting.
- 189-190. Election and Appointment of Officers and Agents.
- 191. Qualifications of Directors or Other Officers.
- 192. Powers of Directors.
- 193-194. Directors' Meetings and Resolutions.
- 195-197. Authority of Other Officers and Agents.
- 198. Notice to Officer as Notice to Corporation.
- 199. Contracts between Stockholder and the Corporation.
- 200. Relation between Officers and Corporation.
- 201-202. Contracts or Other Transactions between Officers and the Corporation.
- 203. Liability of Officers to the Corporation.
- 204-205. Remedies against Officers.
- 206. Liability of Officers and Agents on Contracts.
- 207-209. Liability of Corporation for Torts of Officers and Agents.
- 210. Liability of Officers and Agents to Third Persons for Torts.
- 211. Compensation of Officers.
- 212. Removal of Officers and Agents.
- 213. Relation between Officers and Stockholders.

POWERS OF THE MAJORITY OF STOCKHOLDERS.

- 174. As a rule, each shareholder in a corporation is bound by all acts and proceedings, within the scope of the powers and authority conferred by the charter, which shall be adopted or sanctioned by a vote of the majority of the corporation, duly taken and ascertained according to law.
- 175. But, if the charter invests the board of directors or other agents with the power to manage the concerns of the corporation, the power is exclusive, and cannot be controlled or interfered with by the stockholders, their remedy being to elect or appoint new directors or agents.

176. The majority cannot bind the minority by ultra vires acts; nor can they defeat or impair contract rights between the corporation and individual stockholders; nor can they act fraudulently or oppressively, as against the minority.

177. There is much conflict as to the power of the majority to bind a dissenting minority by acceptance of an amendment or alteration of its charter. The position of the courts may be shortly stated thus:

(a) Where the legislature has not reserved the power to amend the charter—

(1) By the weight of authority, the legislature cannot authorize the majority to alter the charter in any material respect, without the consent of the minority.

(2) All the courts agree that it cannot authorize the majority to engage in a new and different enterprise.

(3) Perhaps all the courts agree that immaterial changes may be made, to facilitate carrying out the objects of the corporation.

(4) Some courts hold that a material alteration, if not a great or radical one, may be made to facilitate carrying out the objects of the corporation.

(b) Where the legislature has reserved the power to alter or amend the charter—

(1) Some courts hold that each stockholder impliedly consents that the majority may, under legislative sanction, engage in new enterprises of the same kind as that authorized by the charter.

(2) Other courts hold that the reservation is intended for the benefit of the public, and can be exercised by the state only, and that it can give no greater power to the majority than if it did not exist.

It is a fundamental principle that the majority of the stockholders can regulate and control the exercise of the powers conferred upon a corporation by its charter, and that the majority has the power, by a vote duly taken and ascertained according to the law by which it is governed, to bind the minority by any act or proceeding which is within the powers and authority of the corporation. Each and every shareholder impliedly agrees that the will of the majority shall govern in all matters coming within the limits of the charter or act of incorporation.¹ Thus, the majority of a corporation established solely for private objects, as a manufacturing or trading corporation, may wind up its affairs, close out its business, and sell its property, against the dissent of the minority, whenever, in the exercise of a sound discretion, they find it expedient to do so.²

Of course, the majority of the stockholders have no power to bind the minority by any act or proceeding that is not within the powers conferred upon the corporation by its charter. The majority represents the corporation, and it can legally do nothing that the corporation cannot do under its grant of power. The majority cannot, at least in the absence of legislative authority, binding upon the stockholders, change the articles of association or charter. They cannot, by resolution, dissolve the corporation before expiration of the time fixed in the charter or articles of association, without the consent of all the members, unless express authority is conferred by the charter.³

And, while a majority of the stockholders may bind the individual stockholders in all matters legitimately within the powers of the company, and subject to the law of the land, they cannot impair or defeat contract rights between the corporation and individual stockholders.⁴ Thus, where a corporation has issued to a stockholder a certificate in the form of an ordinary certificate of stock, but containing a promise by the corporation to pay interest thereon until the

¹ *Durfee v. Railroad Co.*, 5 Allen (Mass.) 230, 242, 1 Cumming, Cas. Priv. Corp. 773; *Dudley v. Kentucky High School*, 9 Bush (Ky.) 578, 1 Cumming, Cas. Priv. Corp. 767.

² *Treadwell v. Manufacturing Co.*, 7 Gray (Mass.) 393. But see *Taylor v. Earle*, 8 Hun (N. Y.) 1. As to the power of a corporation to sell its property, and the limitations thereon, see ante, p. 142.

³ *Barton v. Association*, 114 Ind. 226, 16 N. E. 480.

⁴ *Durfee v. Railroad Co.*, supra.

happening of a specified event, it cannot, by vote of a majority of the stockholders, without his consent, oblige him to receive the bond of the corporation, instead of money, for the interest on such certificate.⁵

Nor can the holders of a majority of the stock of a corporation so conduct and manage its affairs in their own interest, or in the interest of others, as to oppress the minority, or commit a fraud upon their rights. If they attempt to do so, a court of equity will, in a proper case, grant relief, at the suit of the minority.⁶ "The holders of a majority of the stock of a corporation may legally control the company's business, prescribe its general policy, make themselves its agents, and take reasonable compensation for their services. But, in thus assuming the control, they also take upon themselves the correlative duty of diligence and good faith. They cannot lawfully manipulate the company's business in their own interests, to the injury of other stockholders."⁷ It is not every question of mere administration or of policy in which there is a difference of opinion among the shareholders that gives the minority a right to claim that the action of the majority is oppressive, and to come into a court of equity for relief. Generally, the will of the majority must govern, if its action is within its corporate powers. "The court," it was said in a New York case, "would not be justified in interfering, even in doubtful cases, where the action of the majority might be susceptible of different constructions. To warrant the interposition of the court in favor of the minority shareholders in a corporation or joint-stock association, as against the contemplated action of the majority, where such action is within the corporate powers, a case must be made out which plainly shows that such action is so far opposed to the true interests of the corporation itself as to lead to the clear inference that no one thus acting could have been influenced by any honest desire to secure such interests, but that he must have acted with an intent to subserve some outside purpose, regardless of the consequences to the company, and in a manner inconsistent with its interests. Otherwise the court might be called upon to balance probabilities of profit-

⁵ *McLaughlin v. Railroad Co.*, 8 Mich. 100.

⁶ *Ante*, p. 389, and cases there cited; *Miner v. Ice Co.*, 93 Mich. 97, 53 N. W. 218, 2 *Cumming, Cas. Priv. Corp.* 234.

⁷ *Meeker v. Iron Co.*, 17 Fed. 48.

able results to arise from the carrying out of the one or the other of different plans proposed by or on behalf of different shareholders in a corporation, and to decree the adoption of that line of policy which seemed to it to promise the best results, or at least to enjoin the carrying out of the opposite policy. This is no business for any court to follow.”⁸

Where Power of Management is in the Directors.

When the charter invests a board of directors or trustees with the power to manage the concerns of the corporation, the power is exclusive in its character. The stockholders, as such, in their collective capacity, can do no corporate act. The directors are their representatives, and they only are authorized to act.⁹ Thus, conferring authority to sell and convey or to lease the property of the corporation, or to execute corporate obligations, is the exercise of a corporate power, and, if the charter requires such powers to be exercised by the board of directors or trustees, such authority cannot be conferred by a stockholders' meeting.¹⁰ Nor can the stockholders, in such a case, control or interfere with the board in the exercise of its powers. The courts will not, even on the petition of a majority of stockholders, compel the board to do an act contrary to its judgment.¹¹

Power to Accept Amendment or Alteration of Charter.

Difficult questions arise as to the power of the majority of the members of a corporation to bind a dissenting minority by acceptance of an act amending or altering the charter. On some points the courts agree, while on others there is a wide difference of opinion, and a conflict in the decisions. We considered in a previous chapter the power of the state to amend a charter irrespective of the consent of the corporation. We are to consider here the power of a majority of the corporation where the legislature merely authorizes a change, leaving it optional with the corporation whether it will make the change, or continue under the original charter.

Even where the legislature has not reserved the power to alter or

⁸ Per Peckham, J., in *Gamble v. Water Co.*, 123 N. Y. 91, 25 N. E. 201.

⁹ *McCullough v. Moss*, 5 Denio (N. Y.) 575.

¹⁰ *Gashwiler v. Willis*, 33 Cal. 11; *Conro v. Iron Co.*, 12 Barb. (N. Y.) 27; *McCullough v. Moss*, 5 Denio (N. Y.) 575.

¹¹ *McCullough v. Moss*, 5 Denio (N. Y.) 575; *Wright v. Lee*, 2 S. D. 596, 51 N. W. 706, 713, 714.

amend a charter, there is nothing to prevent it from doing so with the consent of all the members. It would be just like the case where both parties to a contract rescind it by mutual agreement, and substitute a new contract. It seems clear, however, that the legislature cannot, where it has not reserved the power, alter a charter in any material respect,—that is, make any fundamental change,—if any one of the stockholders or members dissent, for it would thereby impair the obligation of the contract between the dissenting member and the corporation. Nor can it authorize a majority of the members to make the alteration. A person, in becoming a member of a corporation, does not impliedly agree that the majority of the members shall have the power to bind him by alteration of the objects of the incorporation, or by altering his contract of membership. The majority of the members have no more power to alter the charter, and engage in a new or different enterprise, against the dissent of the minority, than two members of a partnership of three would have the power to change the partnership agreement without the consent of the third.

A leading case on this point is *Natusch v. Irving*.¹² In this case a partnership had been formed for life insurance, and, after it was entered into, an act of parliament made it lawful for such a firm to enter upon the business of marine insurance, which was prohibited to them before. A majority of the partners determined to embark in this new business, but Lord Eldon held that they were barred from doing so by the contract of partnership, unless all the partners agreed. And in England the same doctrine has been applied to corporations. And so it has been held in this country.¹³ The legislature, if it has not reserved the power to alter or amend the charter of a corporation, cannot authorize a material or fundamental amendment, and put it in the power of a majority of the members, even by express provision to that effect, to bind the minority against their dissent; for

¹² 2 Coop. t. Cott. 358, Gow, Partn. (3d Ed.) 576, and referred in *Zabriskie v. Railroad Co.*, 18 N. J. Eq. 178, 1 Cumming, Cas. Priv. Corp. 781, 784.

¹³ In *Ashton v. Burbank*, 2 Dill. 435, Fed. Cas. No. 582, 1 Cumming, Cas. Priv. Corp. 902, a charter authorizing a company to transact a "life and accident insurance" business was amended so as to authorize it to do the business of "fire, marine, and inland insurance," and the amendatory act was accepted by a majority of the stockholders. It was held that this released a dissenting member from liability on a note given by him for an assessment on his stock.

this would be to impair the contract between such dissenting members and the corporation, and the act would be unconstitutional.

In *Proprietors of Union Locks & Canals v. Towne*,¹⁴ the original charter of a corporation empowered it to render the Merrimack river navigable between certain points, and for that purpose to purchase lands, not exceeding six acres, and to collect tolls, for 40 years, not averaging over 12 per cent. on the capital invested. Afterwards an amendatory act was passed, on the petition of the corporation, abolishing all limitation upon the amount and duration of the toll collected, and authorizing the corporation to purchase and hold 100 acres of land. It was held that this amendment was a material alteration of the charter, and discharged a dissenting subscriber to stock in the corporation from liability on his subscription. On the same principle it has been held that a subscriber to stock in a railroad company was released from liability on his subscription by an amendment of the charter, without his consent, superadding to the original object of the corporation an authority to establish a line of water communication in connection with the railroad, and to increase the capital stock for that purpose.¹⁵ Like decisions have been made where the charter of a railroad or turnpike corporation was amended so as to allow it to materially change the location of the road;¹⁶ where the capital stock of a corporation was increased from \$50,000 to \$150,000,¹⁷ where railroad corporations were authorized to consolidate;¹⁸ where a railroad company was authorized to extend its road.¹⁹

The general rule, however, seems to be well settled that a member of a corporation cannot claim release from liability on his subscrip-

¹⁴ 1 N. H. 44.

¹⁵ *Hartford & N. H. R. Co. v. Croswell*, 5 Hill (N. Y.) 383, 1 Cumming, Cas. Priv. Corp. 894.

¹⁶ *Middlesex Turnpike Corp. v. Locke*, 8 Mass. 268; *Kenosha, R. & R. I. R. Co. v. Marsh*, 17 Wis. 13, 1 Cumming, Cas. Priv. Corp. 897.

¹⁷ *Hughes v. Manufacturing Co.*, 34 Md. 316, 330. But see *Schenectady & S. P. R. Co. v. Thatcher*, 11 N. Y. 102.

¹⁸ *Clearwater v. Meredith*, 1 Wall. 25; *Kenosha, R. & R. I. R. Co. v. Marsh*, 17 Wis. 13, 1 Cumming, Cas. Priv. Corp. 897; *Mowrey v. Railroad Co.*, 4 Biss. 78, Fed. Cas. No. 9,891.

¹⁹ *Stevens v. Railroad Co.*, 29 Vt. 545. And see *Zabriskie v. Railroad Co.*, post, p. 453. But see *Durfee v. Railroad Co.*, post, p. 452.

tion, or otherwise object, because the majority have made an immaterial alteration or amendment under legislative authority. But there is much diversity of opinion as to what alterations are material or fundamental within the rule. If the alteration does not materially affect the contract between the corporation and its members, the majority have the power to make it under legislative sanction, and they will not be enjoined at the suit of a dissenting member, nor will he be released from liability on his subscription. This principle has been applied to amendatory acts, accepted by the majority, changing the name of the corporation,²⁰ enlarging the time within which a railroad company may commence and complete its road,²¹ or an hotel company may construct its hotel;²² changing to a slight extent the location or grade of the road of a turnpike or railroad company;²³ authorizing the issue of preferred stock for the purpose of raising money;²⁴ increasing the number of directors.²⁵ In the latter case it was said that alterations which change the nature and purposes of the corporation, or of the enterprise for which it was created, are fundamental, while those which work no material change are not fundamental, and that an alteration increasing the number of directors, not being a change of the nature, purpose, or character of the corporation, or of the enterprise, but of the machinery by which that purpose is to be effected, and that enterprise carried on, is not fundamental, and may therefore be accepted by a majority of the stockholders.

Some of the courts have gone further than this, and have held that a majority of the stockholders of a corporation may bind the minority by acceptance of an act materially altering the charter, if the alteration is made in order to facilitate the execution of the object for which the corporation was originally established, and which is beneficial to the stockholders, or clearly not prejudicial, while some have said that

²⁰ Taggart v. Railroad Co., 24 Md. 563; Clark v. Navigation Co., 10 Watts (Pa.) 364.

²¹ Taggart v. Railroad Co., 24 Md. 563; Milford & C. Turnpike Co. v. Brush, 10 Ohio, 111; Agricultural Branch R. Co. v. Winchester, 13 Allen (Mass.) 29.

²² Union Hotel Co. v. Hersee, 79 N. Y. 454.

²³ Milford & C. Turnpike Co. v. Brush, 10 Ohio, 111; Banet v. Railroad Co., 13 Ill. 504; Irvin v. Turnpike Co., 2 Pen. & W. (Pa.) 466.

²⁴ Rutland & B. R. Co. v. Thrall, 35 Vt. 536; Everhart v. Railroad Co., 28 Pa. St. 339.

²⁵ Mower v. Staples, 32 Minn. 284, 20 N. W. 225.

they may make a change if it is not a great or radical one. Such seems to be the rule in New York, Illinois, and Missouri, and it perhaps extends to other states.²⁶ In *Banet v. Alton & S. R. Co.*,²⁷ it was said: "An alteration in a charter may be so extensive as to work a dissolution of the contract of subscription. An amendment which essentially changes the nature or objects of a corporation will not be binding on the stockholders. A corporation formed for the purpose of constructing a railroad cannot be converted into a company to construct an improvement of a different character, without the consent of all the corporators. A road intended to secure the advantages of a particular line of travel and transportation cannot be so changed as to defeat that general object. The corporation must remain substantially the same, and be designed to accomplish the same general purposes and subserve the same general interests. But such amendments of the charter as may be considered useful to the public and beneficial to the corporation, and which will not divert its property to new and different purposes, may be made, without absolving the subscribers from their engagements. The straightening of the line of the road, the location of a bridge at a different place on a stream, or a deviation in the route from an intermediate point, will not have the effect to destroy or impair the contract between the corporation and the subscribers. We regard these conclusions as reasonable and just, and as well calculated to facilitate the construction of improvements and promote the best interests of the public and of stockholders. The incidental benefits which a few subscribers may realize from a particular location ought not to interfere with the general interests of the public and of the great mass of the corporators. These interests of the public and of the corporation may with propriety be consulted and encouraged, especially where the alteration will not operate to depreciate the value of the stock. A shareholder has no cause to com-

²⁶ *Illinois River R. Co. v. Zimmer*, 20 Ill. 654; *Banet v. Railroad Co.*, 13 Ill. 504; *Hartford & N. H. R. Co. v. Croswell*, 5 Hill (N. Y.) 883, 1 Cumming, Cas. Priv. Corp. 894; *Pacific R. R. v. Renshaw*, 18 Mo. 210; *Pacific R. R. v. Hughes*, 22 Mo. 291. It has been held in Pennsylvania that granting additional privileges beneficial to the corporation does not release a subscriber, though it may extend the liabilities of the company. *Gray v. Navigation Co.*, 2 Watts & S. (Pa.) 156; *Clark v. Navigation Co.*, 10 Watts (Pa.) 364.

²⁷ 13 Ill. 504.

plain of the loss of a mere incidental benefit, which formed no part of the consideration of his contract of subscription.”

The question arises whether this doctrine applies where the legislature has reserved the power to alter, amend, or repeal a charter, and offers the corporation an amendment of its charter authorizing it to engage in an enterprise not originally contemplated. On this point the courts do not agree.

Some courts have taken the view that a person who becomes a member of a corporation, when such power has been reserved by the legislature, impliedly agrees that in case an amendment of its charter is offered by the legislature, authorizing it to engage in a new enterprise of the same kind as that authorized by the charter, it shall be for the corporation, as a body, to determine whether it will accept the same, and that the will of the majority shall govern. In *Durfee v. Old Colony & F. R. R. Co.*,²⁸ the legislature, under a reservation of power to alter, amend, or repeal the charter of a railroad company, passed an act authorizing it to engage in a new enterprise in addition to that contemplated by its charter, but of the same kind,—to extend its road,—and the amendment was accepted by vote of a majority of the stockholders. It was held that this was a matter in which the stockholders had impliedly agreed that the will of the majority should govern, and that the action of the majority was binding upon the dissenting minority. “When,” said the court in this case, “it is expressly provided between the legislature, on the one hand, and the corporation, on the other, as part of the original contract of incorporation, that the former may change or modify or abrogate it, or any portion of it, it cannot be said that any contract is broken or infringed when the power thus reserved is exercised with the consent of the artificial body of whose original creation and existence such reservation formed an essential part. The stockholder cannot say that he became a member of the corporation on the faith of an agreement made by the legislature with the corporation that the original act of incorporation should undergo no change except with his assent. Such a position might be asserted with more plausibility if there was an absence of a clause in the original act of incorporation providing for an alteration in its terms. In such a case it might, perhaps, be maintained that

²⁸ 5 Allen (Mass.) 230, 1 Cumming, Cas. Priv. Corp. 773.

there was a strong implication that the charter should remain inviolate, and that the holders of shares invested their property in the corporation relying upon a contract entered into between it and the legislature that the provisions of the act creating it should remain unchanged. But it is difficult to see how such a construction can be put on a contract which contains an express stipulation that it shall be subject to amendment and alteration. If it be asked by whom such amendment or alteration is to be made, the answer is obvious: By the parties to the contract,—the legislature on the one hand, and the corporation on the other; the former expressing its intention by means of a legislative act, and the latter assenting thereto by a vote of the majority of the stockholders, according to the provisions of its charter. It is nothing more than the ordinary case of a stipulation that one of the parties to a contract may vary its terms with the assent of the other contracting party.” There are other cases to the same effect.²⁹

Other courts repudiate this view, and hold that no material change can be made in the charter of a corporation without the consent of all the stockholders, though authorized by the legislature under a reserved power to alter, amend, or repeal the original charter. In *Zabriskie v. Hackensack & N. Y. R. Co.*,³⁰ a railroad company, whose charter was subject to alteration, amendment, or repeal by the legislature, was by an amendatory act authorized to extend its road, and to issue bonds for the purpose of constructing the extension, and secure them by a mortgage on its road and franchises. It was held that this act could not be accepted by the corporation where a stockholder dissented, and the corporation was enjoined, at the suit of a dissenting stockholder, from acting under it. The court said that the reservation by the state of the power to alter, amend, or repeal the charter was for the benefit of the public, and to be exercised by the state only, and was not intended to give a power to one part of the corporators, as against the other, which they did not have before; that the object of the provision was to avoid the rule of the *Dartmouth College Case*,³¹ and not the rule of *Natusch v. Irving*.³²

²⁹ *White v. Railroad Co.*, 14 Barb. (N. Y.) 560; *Schenectady & S. Plank-Road Co. v. Thatcher*, 11 N. Y. 102; *Buffalo & N. Y. C. R. Co. v. Dudley*, 14 N. Y. 336.

³⁰ 18 N. J. Eq. 178, 1 Cumming, Cas. Priv. Corp. 781.

³¹ Ante, p. 202.

³² Ante, p. 448. And see *South Bay Meadow Dam Co. v. Gray*, 30 Me. 547; *Oldtown & L. R. Co. v. Veazie*, 39 Me. 571.

BY-LAWS.

178. Every private corporation for pecuniary profit has the implied power to enact by-laws for its government. But, to be valid, by-laws—

- (a) Must be reasonable.**
- (b) Must not be inconsistent with principles of law, nor contrary to public policy.**
- (c) Must be general, and not directed against particular individuals.**
- (d) Must be consistent with the charter or articles of association, and within the purposes of the corporation.**
- (e) Must not impair vested contract rights of stockholders, either by depriving them of rights, or by imposing additional liabilities.**

179. Authorized by-laws are binding upon all the stockholders, whether they have expressly assented to them, or knew of them, or not.

180. By-laws cannot confer rights, or impose liabilities, upon third persons, without their express or implied consent.

181. By-laws may be altered or repealed by the corporation at pleasure, and they may be waived.

The office of a by-law is to regulate the conduct and define the duties of the members of the corporation to the corporation and between themselves.³³ Every private business corporation has the implied power to make by-laws. The power is often expressly conferred by the charter or by statute, but this is not at all necessary, for the power is always implied.³⁴ Primarily, the power to make by-

³³ *Flint v. Pierce*, 99 Mass. 68.

³⁴ *Sutton's Hospital Case*, 10 Coke. 23a, 30b, 2 Cumming, Cas. Priv. Corp. 14; 1 Bl. Comm. 475, 2 Cumming, Cas. Priv. Corp. 16; 1 Kyd, Corp. 69, 2 Cumming, Cas. Priv. Corp. 17; 2 Kent, Comm. 278; *Norris v. Staps*, Hob. 211a; and cases cited in the following notes.

laws is in the majority of the stockholders. But they, or the charter, may authorize the board of directors to make them.³⁵ They may also, by a by-law, authorize the board to alter or amend by-laws; but the board, under such a power, has no authority to disregard or alter another by-law, which was intended to impose a limitation on their powers.³⁶

By-laws of a corporation must be proved. They cannot be judicially noticed.³⁷ They are to be proved by the records of the corporation, or by secondary evidence if the records cannot be produced.

Validity of By-Laws.

Any by-law prescribing a rule for the government of the corporation is valid if it is reasonable, and if it is not inconsistent with the charter or articles of association, nor contrary to any statute or principle of the common law, and if it does not impair vested rights. The corporation, for instance, may provide by its by-laws for the election or appointment and the removal of officers and agents, and may prescribe and limit their powers and duties.³⁸ So, it may prescribe how and when corporate meetings shall be held, how they shall be conducted, the manner of voting, etc.³⁹ And it may prescribe, for its own protection, reasonable regulations concerning the transfer of shares, if it does not unreasonably restrict the right of transfer.⁴⁰

³⁵ *Cahill v. Insurance Co.*, 2 Doug. (Mich.) 124. If the charter authorizes the directors to adopt by-laws, a majority may do so. *Id.*

³⁶ *Stevens v. Davison*, 18 Grat. (Va.) 819.

³⁷ *Haven v. Asylum*, 13 N. H. 532.

³⁸ *Com. v. Woelper*, 3 Serg. & R. (Pa.) 29; *Burden v. Burden*, 8 App. Div. 160, 40 N. Y. Supp. 499; *Hale v. Mechanics' Mut. Fire Ins. Co.*, 6 Gray (Mass.) 169. They may require officers to give bond. *Savings Bank of Hannibal v. Hunt*, 72 Mo. 597.

³⁹ *State v. Tudor*, 5 Day (Conn.) 329; *In re Election of Directors of Long Island R. Co.*, 19 Wend. (N. Y.) 87; *Com. v. Woelper*, 3 Serg. & R. (Pa.) 29. But a by-law cannot change charter or statutory provisions as to voting, nor deprive members of the right to vote secured to them by their contract of membership. *Brewster v. Hartley*, 37 Cal. 15, 99 Am. Dec. 237; *post*, p. 478. A by-law may give stockholders a vote for each share, contrary to the common-law rule. *Com. v. Detwiller*, 131 Pa. St. 614, 18 Atl. 990. *Contra*, *Taylor v. Griswold*, 14 N. J. Law, 222. A by-law may allow voting by proxy. *Com. v. Detwiller*, *supra*; *State v. Tudor*, *supra*; *People v. Crossley*, 69 Ill. 195. *Contra*, *Taylor v. Griswold*, *supra*.

⁴⁰ *Post*, p. 457.

And corporations other than joint-stock corporations may enact reasonable by-laws providing for the expulsion of members.⁴¹

It is well settled that by-laws, to be valid, must be reasonable, and not in contravention of law. And whether they are so or not is a question for the court to determine.⁴² For instance, they must not be in restraint of trade, nor impose a burden without any apparent benefit.⁴³ Nor is a by-law valid if it is inconsistent with other general principles of law.⁴⁴ A by-law cannot affect the jurisdiction of courts, as fixed by law, nor impair the right to sue.⁴⁵ Nor can it give the corporation the power to declare shares forfeited for nonpayment of calls.⁴⁶

To be reasonable, and therefore to be valid, by-laws must be general; that is, they must not be directed against particular individuals, nor in favor of particular individuals, but must operate equally upon all to whom they may apply. In *Budd v. Multnomah St. Ry. Co.*,⁴⁷ the directors of a corporation passed a resolution to forfeit and sell the shares of a particular individual for nonpayment of assessments, and the sale was sought to be upheld under a statute requiring a by-

⁴¹ Ante, p. 401.

⁴² *Com. v. Worcester*, 3 Pick. (Mass.) 462; *State v. Overton*, 24 N. J. Law, 435; *Sayre v. Association*, 1 Duv. (Ky.) 143; *People v. Young Men's Father Matthew T. A. B. Soc.*, 41 Mich. 67, 1 N. W. 931; *Palmetto Lodge No. 5 v. Hubbell*, 2 Strob. (S. C.) 457; *Vestry of St. Luke's Church v. Matthews*, 4 Desaus. Eq. (S. C.) 578. As to reasonableness of by-laws providing grounds for expulsion of members, see ante, p. 401 et seq.

⁴³ *Matthews v. Associated Press*, 136 N. Y. 333, 32 N. E. 981; *Sargent v. Insurance Co.*, 8 Pick. (Mass.) 90; and cases hereafter specifically referred to. The courts are not as strict now as formerly in holding contracts to be in restraint of trade. See Clark, Cont. 446. In *Matthews v. Associated Press*, supra, it was held that a by-law adopted by the Associated Press of the State of New York, a corporation, whose members are newspaper publishers, prohibiting its members from receiving and publishing the news dispatches of any other news association covering a like territory and organized for a like purpose, was held not to be in unreasonable restraint of trade, nor invalid as restricting the liberty of speech and of the press.

⁴⁴ *Kent v. Mining Co.*, 78 N. Y. 159, 182; *Sayre v. Association*, 1 Duv. (Ky.) 143.

⁴⁵ *Nute v. Insurance Co.*, 6 Gray (Mass.) 174; *Amesbury v. Insurance Co.*, Id. 596.

⁴⁶ *In re Election of Directors of Long Island R. Co.*, 19 Wend. (N. Y.) 37.

⁴⁷ 15 Or. 413, 15 Pac. 659, W. D. Smith, Cas. Corp. 60.

law to authorize such sales. The court held that the resolution was not valid as a by-law, because it was not general. "I think," said Judge Strahan, "that any by-law enacted under this section of the Code, to be reasonable, ought to be general; that is, it ought to affect every delinquent subscriber, and all delinquent stock, alike, and it ought not to be directed against the stock or interests of a particular stockholder. These are essential requisites to a valid by-law." There are many other decisions to the same effect.⁴⁸

A corporation may adopt by-laws imposing reasonable regulations upon the mode of transferring shares, but it cannot prohibit transfers. Nor can it impose unreasonable regulations. It has been held, for instance, that a by-law prohibiting the transfer of stock by a stockholder without the consent of all the stockholders, or of a particular officer, etc., is against public policy and void; and no exception can be made in the application of this rule on the ground that the stockholders are few, and were originally co-partners, and that the one against whom the by-law is invoked consented to and voted for it.⁴⁹

Whether or not, in the absence of express charter or statutory authority, a corporation may, by a by-law, create a lien on its shares for debts due from its stockholders, is a question upon which the courts do not entirely agree. By the weight of authority, under the general power to regulate the manner in which its stock shall be transferred and its business conducted, etc., a by-law creating a lien on shares for debts due from its stockholders will be valid as against

⁴⁸ "It is plain that all corporation by-laws must stand on their own validity, and not on any dispensation granted to members. They cannot be subjected to any conditions which do not apply to all alike, and cannot be compelled to receive, as matter of grace, anything which is matter of right. Neither, on the other hand, should there be personal exemptions of a general nature from any valid regulations that bind the mass of corporators." Per Campbell, C. J., in *People v. Young Men's Father Matthew T. A. B. Soc.*, 41 Mich. 67, 1 N. W. 931.

⁴⁹ *In re Petition of Klaus* (Wis.) 29 N. W. 582. And see *Farmers' & Merchants' Bank of Lineville v. Wasson*, 48 Iowa, 336; *Sargent v. Insurance Co.*, 8 Pick. (Mass.) 90; *Bank of Attica v. Manufacturers' & Traders' Bank*, 20 N. Y. 501; *Moore v. Bank*, 52 Mo. 377; *Johnson v. Laffin*, 5 Dill. 65, Fed. Cas. No. 7,393, 1 Cumming, Cas. Priv. Corp. 608, affirmed 103 U. S. 800; *Chouteau Spring Co. v. Harris*, 20 Mo. 383. Ante, p. 407.

the stockholders, and as against transferees who do not occupy the position of bona fide purchasers.⁵⁰ But such a by-law is not binding upon bona fide purchasers of shares, without notice of it.⁵¹ The New York court, it seems, has held such a by-law invalid for all purposes, in the absence of legislative authority therefor, on the ground that it is unreasonable, not only because it interferes with the common rights of property, and the dealings of third persons, and prevents the free purchase and transfer or delivery of property, but also for the reason that it gives to the corporation a summary remedy which is unknown to the law, and which subjects shares to what is equivalent to an attachment or an execution without judgment or suit.⁵²

In the absence of express authority, a corporation cannot, by a by-law, provide for forfeiture of stock for nonpayment of assessments thereon.⁵³ But it can do so if expressly authorized.⁵⁴

A corporation has no authority to pass by-laws that are inconsistent with the charter or articles of association, or that are beyond the scope of the purposes of the corporation, as expressed in the charter or articles.⁵⁵ Thus, a corporation cannot, by a by-law, acquire a lien on its shares for debts due to it by the stockholders, if it is expressly or impliedly prohibited from acquiring a lien on shares, as are na-

⁵⁰ *Morgan v. Bank*, 8 Serg. & R. (Pa.) 73; *Vansands v. Bank*, 26 Conn. 144; *Lockwood v. Bank*, 9 R. I. 308; *Cunningham v. Trust Co.*, 4 Ala. 652; *St. Louis Perpetual Ins. Co. v. Goodfellow*, 9 Mo. 149; *Child v. Hudson's Bay Co.*, 2 P. Wms. 207; *M'Dowell v. Bank*, 1 Har. (Del.) 27. And see 1 *Thomp. Corp.* § 1032, citing, among other cases, *People v. Crockett*, 9 Cal. 112; *Mechanics' Bank v. Merchants' Bank*, 45 Mo. 513; *Bank of Holly Springs v. Pinson*, 58 Miss. 421; *Planters' & Merchants' Mut. Ins. Co. v. Selma Sav. Bank*, 63 Ala. 585.

⁵¹ *Driscoll v. Manufacturing Co.*, 59 N. Y. 96, 109.

⁵² *Driscoll v. Manufacturing Co.*, *supra*.

⁵³ *Cahill v. Insurance Co.*, 2 Doug. (Mich.) 124; *In re Election of Directors of Long Island R. Co.*, 19 Wend. (N. Y.) 37.

⁵⁴ *Budd v. Multnomah St. Ry. Co.*, 15 Or. 413, 15 Pac. 659, *W. D. Smith, Cas. Corp.* 60.

⁵⁵ *Brewster v. Hartley*, 37 Cal. 15, 99 Am. Dec. 237; *Bergman v. Association*, 29 Minn. 275, 13 N. W. 120; *Kolff v. St. Paul Fuel Exchange*, 48 Minn. 215, 50 N. W. 1036; *Presbyterian Mut. Assur. Fund v. Allen*, 106 Ind. 593, 7 N. E. 317; *Supreme Council v. Perry*, 140 Mass. 580, 5 N. E. 634; *Vestry of St. Luke's Church v. Mathews*, 4 Desaus. (S. C.) 578.

tional banks by the prohibition in the national banking act against making loans on the security of their shares.⁵⁶ Where the charter of a corporation, or a general statute applicable to it, confers power to enact by-laws for certain specified purposes, it cannot enact a by-law for any other purpose. The case is within the rule, "*Expressio unius est exclusio alterius*."⁵⁷ A corporation whose charter vests the management of its affairs in a board of directors cannot, by a by-law, substitute an executive committee for such board.⁵⁸

Nor can a corporation, by a by-law, deprive a stockholder of vested contract rights, to which he is entitled by virtue of his contract of membership, or of any other contract with the corporation, or of any contract with third persons. In other words, a by-law cannot deprive a stockholder of any rights vested in him at the time it is enacted, unless he consents, or unless his contract with the company allows it.⁵⁹ Nor can a by-law impose upon a stockholder, without his consent, any new liability. Thus, where neither the charter of a corporation, nor any general statute, imposes on the individual members a liability to pay its debts, such liability cannot be imposed by a by-law to which he does not consent.⁶⁰ A person becoming a member of a corporation after a by-law has been adopted, prohibiting members from doing certain things, is bound thereby. It is a part of his contract, and he cannot object to it on the ground that it deprives him of vested rights.⁶¹

A by-law which consists of several distinct and independent parts may be valid as to one part, though void as to the others. Thus, where a by-law of a mutual insurance company provided that in case of loss, if the assured should not acquiesce in the determination by the directors of the amount thereof, any action for the loss claimed must be brought within four months after such determination, at a proper

⁵⁶ *Bullard v. Bank*, 18 Wall. 589; *Bank v. Lanier*, 11 Wall. 369; *Conklin v. Bank*, 45 N. Y. 655.

⁵⁷ *Ireland v. Reduction Co. (R. I.)* 32 Atl. 921; ante, p. 128.

⁵⁸ *Temple v. Dodge (Tex. Sup.)* 32 S. W. 514.

⁵⁹ *Bergman v. Association*, 29 Minn. 275, 13 N. W. 120; *Kent v. Mining Co.*, 78 N. Y. 159, 179.

⁶⁰ *Trustees v. Flint*, 13 Metc. (Mass.) 539; *Reid v. Manufacturing Co.*, 40 Ga. 98.

⁶¹ *Matthews v. Associated Press*, 136 N. Y. 333, 32 N. E. 981.

court in the county in which the office of the company was established, it was held valid as to the limitation of time for suing, though void in so far as it affected the jurisdiction of courts.⁶²

Effect as to Stockholders.

Authorized by-laws, if regularly adopted, are binding upon all the stockholders, whether they have signed them, or otherwise expressly assented to them, or not. They are chargeable with notice of them.⁶³ And a stockholder is bound by by-laws adopted before he became a member, though he may not have had actual knowledge of them.⁶⁴ Of course, invalid by-laws do not bind him. Mere failure of a stockholder to object to by-laws that are void because unauthorized under any of the above rules, until an attempt is made to enforce them against him, does not estop him to object to them.⁶⁵

Effect as to Third Persons.

In so far as a by-law of a corporation is in the nature of a contract, the parties thereto are the corporation, upon the one side, and the individual members, upon the other. The right of any third person to establish a legal claim through a by-law depends upon whether he contracted with reference to it. If he did not, then it does not enter into his contract, and he cannot claim the benefit of it. Thus, where the members of a corporation signed a by-law by which they pledged themselves, in their individual as well as their collective capacity, for all moneys that might be loaned to the company, it was held that a person who loaned money to the company could not hold a member individually liable by virtue of the by-law, where there was no evidence that the loan was made on the credit of it.⁶⁶

Nor, on the other hand, can a by-law impose liabilities on third persons who contract with the corporation without reference to it, or deprive third persons of their legal rights against the corporation. Thus, a by-law of a bank cannot take away from a depositor the right to money deposited by him, but which, by mistake of the bank, was

⁶² Amesbury v. Insurance Co., 6 Gray (Mass.) 506.

⁶³ McFadden v. Board, 74 Cal. 571, 16 Pac. 397; Palmetto Lodge v. Hubbell, 2 Strob. (S. C.) 457.

⁶⁴ Matthews v. Associated Press, 136 N. Y. 333, 32 N. E. 981.

⁶⁵ Kolff v. Fuel Exchange, 48 Minn. 215, 50 N. W. 1036.

⁶⁶ Flint v. Pierce, 99 Mass. 68.

not credited to him.⁶⁷ Nor can a corporation bind a bona fide purchaser of certificates of stock by a by-law, of which he has no notice, reserving a lien on the shares for an indebtedness due from the holder.⁶⁸ Nor are persons dealing with an agent of a corporation bound by a by-law limiting the apparent authority with which the corporation has clothed him.⁶⁹

If a person enters into a contract with a corporation, with notice of a by-law, and does not, by special contract, exclude it, the by-law forms a part of his contract. Thus, where a person entered into the employ of a corporation at a yearly salary, without any special contract as to the term of service, and continued in its service with notice of a by-law providing that his office should be held at the pleasure of the board of directors, he was held bound thereby.⁷⁰ It is otherwise, however, where the by-law is excluded by the terms of the contract, as it would be, in the case mentioned, by a special contract for a certain term.⁷¹

Repeal and Amendment of By-Laws.

A corporation generally has the power to repeal by-laws and enact new ones at pleasure,⁷² but the power to alter by-laws has the same limits as the power to make them in the first instance. These limitations have just been pointed out. The power to make by-laws, as we have seen, is to make such only as are not inconsistent with the constitution of the corporation and the law. And a by-law cannot impair vested rights of a stockholder. So, alteration of a by-law is invalid if it contravenes these rules. Thus, where a by-law divided the stock of a corporation into equal shares, giving equal rights, and the stock was thus issued, a new by-law providing for the surrender of shares, and issue of preferred stock instead, on payment of a certain additional sum, was held void, as against dissenting stockholders, because it im-

⁶⁷ *Mechanics' & Farmers' Bank v. Smith*, 19 Johns. (N. Y.) 115.

⁶⁸ *Driscoll v. Manufacturing Co.*, 59 N. Y. 96, 109.

⁶⁹ *Rathbun v. Snow*, 123 N. Y. 343, 25 N. E. 379.

⁷⁰ *Douglass v. Insurance Co.*, 118 N. Y. 484, 23 N. E. 806.

⁷¹ *Trustees of Soldiers' Orphans' Home v. Shaffer*, 63 Ill. 243; *Martino v. Insurance Co.*, 47 N. Y. Super. Ct. 520.

⁷² See *Smith v. Nelson*, 18 Vt. 511; *Underhill v. Improvement Co.*, 93 Cal. 300, 28 Pac. 1049.

paired their vested rights under the contract with the corporation under which they took their shares.⁷³

Though, as we have seen, the directors may, by a by-law, be given the power to enact and to alter and amend by-laws, they have no authority, under such a power, to disregard or alter another by-law which was intended as a limitation on their powers.⁷⁴

Waiver of By-Law.

A by-law may not only be repealed, but it may be waived, by the corporation. If a course of action contrary to a by-law of a private corporation is acquiesced in by the shareholders, the by-law is thereby waived, and will not affect the rights of persons dealing with the corporation in good faith.⁷⁵ This is true, even though they may be shareholders, if they did not have actual notice of the by-law.⁷⁶ And acts of the directors in violation of the by-laws may be ratified by the shareholders, and generally by the same number of shareholders as would be necessary to enact them.⁷⁷ But the officers of a corporation cannot waive by-laws adopted by the stockholders for the protection of the corporation.⁷⁸

STOCKHOLDERS' MEETINGS.

182. A majority of the stockholders can bind the corporation only at a meeting regularly held and conducted. To constitute a legal meeting, so as to render the acts and vote of the majority binding:

- (a) The meeting must be regularly called by one having authority. In the absence of provision to the contrary, such authority exists in the directors or managing agents.
- (b) Notice of the time and place of meeting must be given to each stockholder, unless the time and

⁷³ Kent v. Mining Co., 78 N. Y. 159, 182.

⁷⁴ Stevens v. Davison, 18 Grat. (Va.) 819.

⁷⁵ Clark v. Insurance Co., 6 Cush. (Mass.) 342; Susquehanna Mut. Fire Ins. Co. v. Elkins, 124 Pa. St. 484, 17 Atl. 24.

⁷⁶ Underhill v. Improvement Co., supra.

⁷⁷ Underhill v. Improvement Co., 93 Cal. 300, 28 Pac. 1049.

⁷⁸ Mulrey v. Insurance Co., 4 Allen (Mass.) 116; Hale v. Insurance Co., 6 Gray (Mass.) 169.

place are definitely fixed by statute, or by the charter or by-laws, or by usage. But if all the stockholders are present, in person or by proxy, want of notice is immaterial.

- (c) If the meeting is special, notice of the business to be transacted must be given. It is otherwise where the meeting is general; that is, for the transaction of any business within the powers of the corporation.
- (d) The meeting must be held at a reasonable time and place. It cannot be held out of the state, without the consent of all the stockholders; nor, perhaps, should it be so held with their consent unless allowed by statute. But, in the absence of express prohibition, those who participate in such a meeting cannot question its legality.
- (e) The meeting must be regularly conducted.
- (f) If a statute or the charter or by-law provides that a certain number of stockholders shall be necessary to constitute a quorum for the transaction of business, a less number cannot act, but may adjourn. In the absence of express provision, no particular number is necessary to constitute a quorum.
- (g) The major part of the legal votes actually cast at a meeting constitutes a "majority," and prevails.
- (h) A meeting and proceedings are not rendered illegal by the fact that one of the stockholders is non compos mentis, or otherwise under legal disability.
- (i) Meetings are presumed to have been regular, and to have been legally conducted, unless the contrary appears.

183. An adjourned meeting is merely a continuation of the original meeting, without any loss or accumulation of powers.

184. A court of equity has jurisdiction to supervise and control an election, and appoint a master for that purpose, when necessary to procure a fair election.

In order that the acts of a majority of the stockholders may be binding on the corporation, they must be done at a meeting of the stockholders. It is only at a meeting duly held and regularly conducted that the stockholders represent the corporation.⁷⁹ Thus, the assent of a majority of the stockholders to the appointment of an agent to execute a mortgage on behalf of the corporation, if expressed elsewhere than at a meeting, as where the assent of each is given separately, and at different times, to a person who goes to them privately, is a nullity, and a mortgage given in pursuance thereof is void.⁸⁰

Calling Meetings.

It is generally expressly provided by the charter or by-laws who shall call stockholders' meetings, and no meeting can be legally called except in compliance therewith. If the charter and by-laws are silent on the subject, a meeting may be called by the directors or the general agent to whom is intrusted the management and control of its affairs, whenever, in their opinion, the condition and affairs of the corporation are such as to render a meeting necessary.⁸¹ If all the stockholders are present at a meeting, the fact that it was called by one not authorized will not render the proceedings invalid. If the proper officers refuse to perform their duty, positively imposed by law, to call a meeting of stockholders for an election of directors, a stockholder may compel such performance by mandamus.⁸²

Notice of Meeting.

It is essential to the validity of a stockholders' meeting, and of the acts and votes of the majority thereat, that due notice of the day, hour, and place of the meeting shall have been given personally to each stockholder, unless the stockholders were in fact all present, in person, or by proxy, or unless the time and place of the meeting

⁷⁹ *Duke v. Markham*, 105 N. C. 138, 10 S. E. 1003; *Peirce v. Building Co.*, 9 La. 397; *Sayles v. Brown*, 40 Fed. 8.

⁸⁰ *Duke v. Markham*, *supra*.

⁸¹ *Stebbins v. Merritt*, 10 Cush. (Mass.) 27, 33.

⁸² *People v. Cummings*, 72 N. Y. 433.

were definitely fixed by statute, or by the charter or by-laws of the company, or by usage.⁸² It is not enough to give notice of the day. The notice must also specify the hour.⁸⁴ If the meeting is a stated one,—that is, if the time and place of holding the same are fixed by the charter or by-laws, or by statute or usage,—no notice is required of the time and place of holding it.⁸⁵ It is immaterial in what way the time and place of a general meeting are fixed. If they have been fixed by usage, a tacit understanding of the members, or in any other way, it is enough.⁸⁶ The fact that a by-law fixes the day and place for an annual meeting does not dispense with the necessity for notice, for the stockholders are entitled to notice of the hour.⁸⁷

If the meeting is a special one, notice must be given to each stockholder, not only of the time and place of meeting, but also of the business which will be transacted, and there will be no power to transact any other business.⁸⁸ But, if the meeting is a general one,—that is, for the transaction of all business within the powers of the corporation,—such notice is not necessary.⁸⁹ Stated meetings are to be regarded as general ones, unless restricted by statute or by the charter or by-laws.⁹⁰

If all the stockholders have been notified, and are present at the meeting, in person or by lawful proxy, and no objection is then made to the regularity of the notification, all objections on that ground are waived.⁹¹ Indeed, the presence of all the stockholders would obviate the objection that there was no notice.⁹² Acts of the majority

⁸² *Stow v. Wyse*, 7 Conn. 214, 18 Am. Dec. 99, and note; *Wiggin v. Elder, etc.*, 8 Metc. (Mass.) 301; *San Buenaventura Commercial Min. & Manuf'g Co. v. Vassault*, 50 Cal. 534. See *State v. Bonnell*, 35 Ohio St. 10.

⁸⁴ *San Buenaventura Commercial Min. & Manuf'g Co. v. Vassault*, 50 Cal. 534.

⁸⁵ *Warner v. Mower*, 11 Vt. 385; *Atlantic Mut. Fire Ins. Co. v. Sanders*, 36 N. H. 252, 269. And see *State v. Bonnell*, 35 Ohio St. 10, 15.

⁸⁶ *Atlantic Mut. Fire Ins. Co. v. Sanders*, 36 N. H. 252, 269.

⁸⁷ *San Buenaventura Commercial Min. & Manuf'g Co. v. Vassault*, 50 Cal. 534.

⁸⁸ *Warner v. Mower*, 11 Vt. 385; *People's Mut. Ins. Co. v. Westcott*, 14 Gray (Mass.) 440; *Atlantic De Laine Co. v. Mason*, 5 R. I. 463; *Evans v. Heating Co.*, 157 Mass. 37, 31 N. E. 698.

⁸⁹ *Warner v. Mower*, 11 Vt. 385. See *People v. Batchelor*, 22 N. Y. 128, 131.

⁹⁰ *Warner v. Mower*, 11 Vt. 385.

⁹¹ *Stebbins v. Merritt*, 10 Cush. (Mass.) 27, 34.

⁹² See *People v. Peck*, 11 Wend. (N. Y.) 604, 611.

at a meeting that was irregular for want of notice may be ratified by the majority at a subsequent meeting that is regular.⁹³

Time and Place of Meeting.

Meetings cannot be held at an unreasonable or inconvenient time or place. If a particular time or place is fixed by the charter or by-laws, or by statute, the provisions must be observed. Some of the courts have held that, as a corporation has no legal existence beyond the limits of the state by which it was created,⁹⁴ neither the stockholders nor the directors of a corporation can hold a meeting, and do strictly corporate acts, outside the state. This proposition has been laid down broadly and without qualification. The leading case on this point is *Miller v. Ewer*.⁹⁵ In this case, under a charter granted by the state of Maine, the incorporators met in the state of New York, and there organized and accepted the charter, and elected officers and directors. The directors then met in the city of New York, and authorized the president and secretary to execute a mortgage on the corporate property, which was done accordingly. It was held that the action of the incorporators in meeting and electing directors was a corporate act, and could not be performed outside of the state of Maine, that the directors were not legally chosen, and that the mortgage, therefore, was void. The incorporators, it was said, as natural persons, have no power to bring the corporation, the artificial being, into life and active operation. "The charter confers upon them a new faculty for this purpose,—a faculty which they can have only by virtue of the law which confers it. That law is inoperative beyond the bounds of the legislative power by which it is enacted. As the corporate faculty cannot accompany the natural persons beyond the bounds of the sovereignty which confers it, and they cannot possess or exercise it there, [they] can have no more power there to make the artificial being act, than other persons not named or associated as incorporators. Any attempt to exercise such a faculty there is merely a usurpation of authority by persons destitute of it, and acting without any legal capacity to act in that manner. It follows that all votes and proceedings of per-

⁹³ *Richardson v. Railroad Co.*, 44 Vt. 613; *Jones v. Turnpike Co.*, 7 Ind. 547.

⁹⁴ Ante, p. 74.

⁹⁵ *Miller v. Ewer*, 27 Me. 509.

sons professing to act in the capacity of corporators, when assembled without the bounds of the sovereignty granting the charter, are wholly void." ⁹⁶

It will be noticed that in this case the corporators named in the charter met and organized outside the state granting the charter. They did not meet and organize in the state, and then hold a meeting outside the state for the election of the directors. The decision, therefore, might well have been based on the ground that the corporation had not been legally organized, leaving untouched the question whether the stockholders of a corporation which has been duly and legally organized within the state may hold meetings and transact corporate business in another state. The weight of modern authority seems strongly in favor of holding such a meeting, if held with the consent of all the stockholders, and if there is no express prohibition in the charter or by-laws, or in some statute, not absolutely void, but, at most, merely irregular. In *Ohio & M. R. Co. v. McPherson*,⁹⁷ the stockholders of an Illinois corporation, which had been duly organized in that state, held meetings and transacted corporate business in Missouri; and subscribers sought to defeat an action on their subscriptions on the ground that the calls for stock assessments were made in Missouri, and the votes and proceedings of the stockholders and directors in that state were void. It was held that the defense could not be sustained. "After the corporation had become full-fledged," it was said, "I see nothing in reason or principle why the stockholders could not as well elect directors, as the directors elect a treasurer, on the Missouri side of the line. The most that could be said, under such circumstances, is that the election was irregular. The corporation having once been put into existence, if the members of the board of directors, whether charter members, or their appointees, or those elected by the stockholders in St. Louis, accepted their office, and acted under their appointment or election, as the evidence shows was the case, they became de facto directors, and their authority to act on behalf of the corporation could not be questioned by the appellants, in this collateral suit,

⁹⁶ And see *Bellows v. Todd*, 39 Iowa, 209, 217; *Ormsby v. Mining Co.*, 56 N. Y. 623; *Franco-Texan Land Co. v. Laigle*, 59 Tex. 339.

⁹⁷ 35 Mo. 13.

without showing a judgment of ouster against them in a direct proceeding by the government for that purpose.”⁹⁸

It has also been held by the supreme court of the United States that where a stockholders' meeting is held in a state other than that by which the corporation was created, and all the stockholders are present and take part, they and the corporation are estopped to question the validity of the proceedings.⁹⁹ Mr. Morawetz says that “there is no objection to a meeting held in a foreign jurisdiction, provided all the shareholders give their consent. And, in the absence of an express statutory prohibition, there appears to be no reason why the shareholders in an ordinary business corporation should not provide in their articles of association that meetings may be called at convenient places outside of the state under whose laws the company is formed.”¹⁰⁰ Meetings cannot be held in another state unless all the stockholders consent, nor if, as is sometimes the case, such meetings are expressly prohibited by statute, or by the charter or by-laws.¹⁰¹ A meeting in one of several states of the stockholders of a corporation chartered in all of those states is valid, in respect to the property of the corporation in all of the states, without the necessity of a repetition of the meeting in the other states.¹⁰²

Conduct of the Meeting.

Of course, the meeting must be conducted regularly and fairly, and regulations contained in the charter or by-laws must be observed.¹⁰³ But it is not every slight and immaterial irregularity that will vitiate the proceedings. Thus, the fact that the inspectors at a stockholders' meeting are not sworn, or are not sworn in the proper manner, will

⁹⁸ And see *Wright v. Lee*, 2 S. D. 596, 51 N. W. 706, 714.

⁹⁹ *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855; *Heath v. Smelting Co.*, 39 Wis. 146.

¹⁰⁰ 1 Mor. Priv. Corp. § 488.

¹⁰¹ In *Hodgson v. Railroad Co.*, 46 Minn. 454, 49 N. W. 197, it was held that a general stockholders' meeting for the election of officers held out of the state, all of the stockholders not consenting, and the by-laws providing that it shall be held at a specified place in the state, is illegal; and, as against the officers thus elected, those previously in office have the right to retain control of the affairs of the corporation. And see *Ormsby v. Mining Co.*, 56 N. Y. 623.

¹⁰² *Graham v. Railroad Co.*, 118 U. S. 161, 6 Sup. Ct. 1009.

¹⁰³ See *Sayles v. Brown*, 40 Fed. 8.

not invalidate an election, if no objection is interposed at the time of the election. It is enough that they are duly appointed and enter on the discharge of their duties, and are therefore inspectors de facto.¹⁰⁴

It is not necessary, in the absence of some express requirement, that the clerk, moderator, inspector, or chairman chosen to preside over a stockholders' meeting shall be a stockholder or member. He acts merely as an agent of the corporation, to preside and see that the proceedings are conducted in a legal and orderly manner; and there is nothing in the nature of the office which requires him to be a member, although, from convenience, the usage is to select one of the members to perform the duty.¹⁰⁵ Statutory or charter requirements, however, in this respect must be observed.¹⁰⁶

"Quorum" and "Majority."

By the term "quorum" is meant the number of members of a corporation, board, committee, etc., who must be present in order to take action. Generally, by statute, or by particular charters or by-laws, persons owning a majority of the shares must be present or represented at a stockholders' meeting, to constitute a quorum, and, unless there is a quorum present, no action can be taken. Less than a quorum can do no more than adjourn. A majority of the legal votes actually cast, a quorum being present, will bind the corporation.

At common law no particular number of stockholders need be present, except that there must be at least two, for one person could not hold a meeting. If all the stockholders have been duly notified, or if the meeting is a stated one, those who assemble, though they represent less than a majority of the shares, constitute a quorum, and may act, unless there is express provision to the contrary, and a majority of these, however few, may bind the corporation. At common law, therefore, the "majority of the stockholders," as the term is used in reference to its power to bind the corporation, does not necessarily mean persons representing a majority of the shares, or a majority of persons owning shares. It means, in the absence of a provision to

¹⁰⁴ In re Election of Directors of Mohawk & H. R. Co., 19 Wend. (N. Y.) 135; In re Election of Directors of Chenango County Mut. Ins. Co., Id. 635.

¹⁰⁵ Stebbins v. Merritt, 10 Cush. (Mass.) 27, 34.

¹⁰⁶ See People v. Peck, 11 Wend. (N. Y.) 604.

the contrary, the major part of those who are present at a regular corporate meeting. "There is a distinction taken between a corporate act to be done by a select and definite body, as by a board of directors, and one to be performed by the constituent members. In the latter case a majority of those who appear may act, but in the former a majority of the definite body must be present, and then a majority of the quorum may decide. This is the general rule on the subject, and, if any corporation has a different modification of the expression of the binding will of the corporation, it arises from the special provisions of the act or charter of incorporation."¹⁰⁷

At a valid stockholders' meeting, the charter and by-laws being silent on the subject, a majority of the votes cast, though but a minority of the stock represented, prevails. Those having an opportunity to vote, and not voting, are held to acquiesce in the result of the votes actually cast. Therefore, if some of the members become dissatisfied, and fail or refuse to vote, a majority of the legal votes actually cast, though less than a majority of all the votes represented at the meeting, will elect.¹⁰⁸

Disability of Individual Stockholders.

If all of the stockholders are present, or have been duly notified, the meeting and proceedings are not rendered illegal by the fact that one of them is non compos mentis, or otherwise under legal disability. The law does not look into the capacity of the stockholders to transact business, but only regards the capacity of the aggregate body when duly assembled. "If it were otherwise," said Bigelow, J., "the legal incapacity of a stockholder, such as coverture, infancy, or insanity, would operate as an effectual obstacle to a valid assembly of any aggregate corporation. The law confers the attribute of individual-

¹⁰⁷ 2 Kent, Comm. 293; 1 Kyd, Corp. 401; Ex parte Willcocks, 7 Cow. (N. Y.) 402, 410; Field v. Field, 9 Wend. (N. Y.) 394, 403.

¹⁰⁸ First Parish in Sudbury v. Stearns, 21 Pick. (Mass.) 148; State v. Chute, 34 Minn. 135, 24 N. W. 353. See, contra, Com. v. Wickersham, 66 Pa. St. 134. In this case, at a convention of school directors, 112 were present. Of these, 56 voted for one candidate for superintendent, while 55 voted for another, and one refused to vote at all. It was held that the former did not have a majority of the directors present, as the director not voting was entitled to be counted as present, and was not to be considered as absent, and the legal intendment was that he voted for neither or for the minority candidate.

ity on the entire body constituting a corporation, and in which the individuals composing it are merged. When duly assembled, the corporation itself becomes the individual or person whose acts and proceedings the law can alone regard. If, therefore, it is legally called together, the law presumes that the individual members are competent to the transaction of business.”¹⁰⁹

Record and Proof of Action.

In the absence of express requirement to the contrary in the charter or by-laws, the resolutions adopted at a stockholders' meeting need not be recorded in the books of the corporation. In the absence of a record of the proceedings, they may be proved by parol evidence.¹¹⁰

Cure of Irregularity by Ratification.

If a stockholders' meeting is irregularly called or conducted, the irregularity may generally be waived by the stockholders. They may ratify acts of the majority which are not binding because of irregularities, and thereby render them binding.¹¹¹

Presumption of Regularity.

Every reasonable intendment is to be made in favor of the regularity of stockholders' meetings, and the burden is upon one who claims that they were invalid to show the circumstances rendering them so. In the absence of evidence to the contrary, their legality will be presumed. “The maxim of law in such cases is, ‘Omnia rite acta presumuntur.’”¹¹² Thus, it has been held that, in the absence of evidence to the contrary, it will be presumed that due notice was given to all the stockholders.¹¹³ So, where the by-laws of a corporation required the meetings to be held at the counting room of the company, and it appeared from the records that a meeting was held at the dwelling house of the general agent, without stating that it was at the counting room, it was presumed that the counting room was, for

¹⁰⁹ *Stebbins v. Merritt*, 10 Cush. (Mass.) 27, 33.

¹¹⁰ *Handley v. Stutz*, 139 U. S. 417, 11 Sup. Ct. 530, 1 Cumming, Cas. Priv. Corp. 855.

¹¹¹ *Richardson v. Railroad Co.*, 44 Vt. 613; *Jones v. Turnpike Co.*, 7 Ind. 547.

¹¹² *Citizens' Mut. Fire Ins. Co. v. Sortwell*, 8 Allen (Mass.) 217.

¹¹³ *Sargent v. Webster*, 13 Metc. (Mass.) 497.

the time being, at such place.¹¹⁴ So, it will be presumed that a quorum of members was present, unless the contrary clearly appears.¹¹⁵

Adjourned Meetings.

A corporation may transact any business at an adjourned meeting that could have been transacted at the original meeting, for it is but a continuation of the same meeting. Whether the meeting is continued without interruption for many days, or by adjournment from day to day, or from time to time, many days intervening, it must be considered the same meeting, without any loss or accumulation of powers.¹¹⁶

Equity Jurisdiction.

A court of equity has jurisdiction to supervise and control an election of directors, and to appoint a master for that purpose, when it appears that through fraud, violence, or other unlawful conduct on the part of a portion of the corporators, a fair and honest election cannot be held without the court's interposition.¹¹⁷

It has been held that, if an election is held illegally, a court of equity has jurisdiction to set it aside at the suit of a dissenting stockholder.¹¹⁸ But, by the better opinion, some other ground for equitable relief must exist, for otherwise the remedy at law by quo warranto would be adequate. A court of equity will not primarily take jurisdiction to determine the legality of an election of directors, or to remove a director who is in possession of the office. It will inquire into the regularity of the election, or the right of the person to the office, only when the question arises incidentally and collaterally in a suit of which the court has rightful jurisdiction, and when the grant of the relief depends upon its decision.¹¹⁹

¹¹⁴ *McDaniels v. Manufacturing Co.*, 22 Vt. 274.

¹¹⁵ *Citizens' Mut. Fire Ins. Co. v. Sortwell*, 8 Allen (Mass.) 217.

¹¹⁶ *Warner v. Mower*, 11 Vt. 385; *Smith v. Law*, 21 N. Y. 296. And see *Schoff v. Town of Bloomfield*, 8 Vt. 472.

¹¹⁷ *Tunis v. Railroad Co.*, 149 Pa. St. 70, 24 Atl. 88.

¹¹⁸ *Wright v. Water Co.*, 67 Cal. 532, 8 Pac. 70.

¹¹⁹ *Perry v. Oil-Mill Co.*, 93 Ala. 364, 9 South. 217; *Nathan v. Tompkins*, 82 Ala. 437, 2 South. 747.

SAME—VOTING.

185. Unless the right is taken away by express charter or statutory provision, or by the agreement under which shares were acquired, every stockholder is entitled to vote at corporate meetings; and he cannot be deprived of the right by by-laws enacted after his shares were acquired. The following rules may be particularly mentioned:

- (a) Ordinarily the holder of the legal title on the books of the corporation is entitled to vote.
- (b) The pledgor of shares, if he retains the title, is entitled to vote.
- (c) A trustee who holds the legal title, and not the cestui que trust, is entitled to vote.
- (d) Stock held by the corporation itself cannot be voted.
- (e) Shares held by two or more jointly, either in their own right, or as executors, trustees, etc., cannot be voted unless all agree upon the vote.
- (f) The right may be restricted by statute, and the statute cannot be evaded by transfer of the bare legal title.
- (g) Personal interest in a measure does not disqualify a stockholder from voting.

186. NUMBER OF VOTES—At common law each shareholder had only one vote, without regard to the number of shares owned by him. But now, generally by charter or statutory provision, and perhaps by custom, there is a right to one vote for each share. Sometimes, by statute, a single stockholder is restricted as to the number of votes, and he cannot evade the statute by a colorable transfer.

187. CUMULATIVE VOTING—Cumulative voting is allowed in some states by statute, but the right does not exist at common law.

188. PROXY—At common law the right to vote can only be exercised in person; but the right to vote by proxy—that is, by another under a power of attorney—is generally given by statute, or by the charter or by-laws. In regard to proxies, the following points may be particularly mentioned:

- (a) A proxy can only be given by the legal owner of stock at the time the vote is cast.
- (b) An agreement not to give a proxy is contrary to public policy, and therefore void.
- (c) A proxy, though in terms irrevocable, may nevertheless be revoked, if not coupled with an interest. Some courts hold such a proxy void as against public policy.

Who Entitled to Vote.

Every stockholder has, as incident to his ownership of stock, a right to vote at stockholders' meetings, unless he is prohibited from doing so by some express charter or statutory provision, or by the agreement under which he holds his shares. He cannot be deprived of this right by a by-law, unless such a by-law is expressly authorized in advance, or where it was enacted before he acquired his shares.¹²⁰ But there is nothing to prevent a corporation, on issuing stock, common or preferred, after its organization, from stipulating that the holders shall not have or exercise the right to vote the same.¹²¹

The general rule is that the holder of the legal title to shares is entitled to vote them. And, in case of a dispute as to the right to vote at a stockholders' meeting, the books of the corporation are prima facie evidence as to who possesses that right.¹²² The inspectors of election are not to inquire beyond the transfer book. Any private agreement or understanding between the individual holding the legal title to the stock in due form and others is a matter between themselves, with which the corporation has no concern.¹²³

¹²⁰ Ante, p. 455, note 89.

¹²¹ *Miller v. Ratterman*, 47 Ohio St. 141, 24 N. E. 496.

¹²² *Hoppin v. Buffum*, 9 R. I. 513, 518; *Com. v. Dalzell*, 152 Pa. St. 217, 25 Atl. 535; *Pender v. Lushington*, 6 Ch. Div. 70.

¹²³ *In re Long Island R. Co.*, 19 Wend. (N. Y.) 37, 44.

Same—Pledgor and Pledgee.

A person who pledges his stock is entitled to vote upon it until the title of the pledgee to the stock is perfected.¹²⁴ And it has been held that, if the stock stands on the books of the corporation in the name of the pledgee, the pledgor may, by suit in equity, compel a transfer to him, or oblige the pledgee to give him a proxy to vote.¹²⁵ But if the pledgor acquiesces in the control of the stock by the pledgee, who appears as the record owner, and makes no effort to inform the corporation of his ownership until a contested election occurs, and then not until the votes have been, or are being, counted, it will be too late to ask a court of equity to interfere with the declared result of the election.¹²⁶ So long as the stock stands on the books of the corporation in the name of the pledgee, without any reservation to the pledgor of the right to vote the same, the pledgee is entitled to vote.¹²⁷

Same—Trustees.

One in whose name stock stands on the books of the corporation as trustee is entitled to vote upon it, unless the cestui que trust seasonably asserts his right to have it transferred to him.¹²⁸

Same—Shares Held by the Corporation.

A corporation cannot hold its own stock so as to entitle its directors or trustees to vote upon it.¹²⁹ Nor can persons who hold stock in trust for the benefit of the corporation vote thereon. The right to vote the stock is suspended while it is so held.¹³⁰

¹²⁴ *McDaniels v. Manufacturing Co.*, 22 Vt. 274; *President, etc., of Merchants' Bank v. Cook*, 4 Pick. (Mass.) 405; *In re Barker*, 6 Wend. (N. Y.) 509; *Ex parte Willcocks*, 7 Cow. (N. Y.) 402; *Hoppin v. Buffum*, 9 R. I. 513.

¹²⁵ *Vowell v. Thompson*, 3 Cranch, C. C. 428, Fed. Cas. No. 17,023; *Hoppin v. Buffum*, 9 R. I. 513.

¹²⁶ *Hoppin v. Buffum*, 9 R. I. 513.

¹²⁷ See *Com. v. Dalzell*, 152 Pa. St. 217, 25 Atl. 535.

¹²⁸ *Hoppin v. Buffum*, 9 R. I. 513; *In re Barker*, 6 Wend. (N. Y.) 509; *Com. v. Dalzell*, 152 Pa. St. 217, 25 Atl. 535. And see *Wilson v. Proprietors Central Bridge*, 9 R. I. 590.

¹²⁹ *Ex parte Holmes*, 5 Cow. (N. Y.) 426. And see *Vail v. Hamilton*, 85 N. Y. 453.

¹³⁰ *American Railway-Frog Co. v. Haven*, 101 Mass. 398. And see *State v. Smith*, 48 Vt. 266.

Same—Shares Owned Jointly.

Since the right of voting upon stock is in the legal owner, it follows that stock held jointly by two or more persons, either in their own right, or as executors, trustees, etc., cannot be voted at all, unless all agree upon the vote.¹³¹

Same—Restrictions in Charter or Statute.

The right to vote may be restricted by the charter or by statute. Sometimes it is expressly provided, for instance, that nonresident stockholders of particular corporations shall not be allowed to vote at meetings of the corporation. The object of such a provision is to prevent corporations from being controlled by nonresidents.¹³² And often the number of votes which a single stockholder shall be allowed to cast is limited. The object is to prevent the corporation from getting into the control of a single person.¹³³

Same—Evasion of Statutory or Charter Prohibition.

Where, by statute or by the charter, particular stockholders are prohibited from voting, the prohibition cannot be evaded by transferring the stock to others merely for the purpose of enabling them to vote upon it. Thus, where the charter of a corporation provided that no stockholder should be entitled to cast more than one-fourth of all the votes at an election of directors, it was held that a stockholder who owned more than one-fourth of the shares could not gratuitously transfer part of the stock for the purpose of enabling the transferees to vote it, and such transferees were enjoined from voting at the suit of another stockholder.¹³⁴ So, where nonresident stockholders in banking corporations were prohibited from voting, it was held that the prohibition could not be evaded by gratuitously transferring stock to residents for the purpose of enabling them to vote upon it. "The law," it was said, "is not to be outwitted by cunning devices."¹³⁵

¹³¹ *Tunis v. Railroad Co.*, 149 Pa. St. 70, 24 Atl. 88.

¹³² *State v. Hunton*, 28 Vt. 594.

¹³³ *Mack v. Iron Co.*, 90 Ala. 396, 8 South. 150.

¹³⁴ *Mack v. Iron Co.*, 90 Ala. 396, 8 South. 150; *Campbell v. Poultney*, 6 Gill & J. (Md.) 94; *Webb v. Ridgely*, 38 Md. 364. Contra, *Pender v. Lushington*, L. R. 6 Ch. Div. 70.

¹³⁵ *State v. Hunton*, 28 Vt. 594.

Same—Personal Interest of Stockholder.

The fact that a stockholder has a personal interest in a matter coming before a stockholders' meeting, different from that of the other stockholders, does not disqualify him from voting. "A shareholder has a legal right, at a meeting of the shareholders, to vote upon a measure, even though he has a personal interest therein separate from other shareholders. In such a meeting each shareholder represents himself and his own interests solely, and he in no sense acts as a trustee or representative of others."¹³⁶ In *Northwest Transp. Co. v. Beatty*,¹³⁷ one of the directors in a corporation contracted with his colleagues to sell to the company a vessel which he owned, at a certain price. The contract, though fair, was voidable, but it was subject to ratification by the stockholders; and it was held that the vendor director had a right, at a meeting of the stockholders, to vote in favor of ratifying the contract and concluding the purchase, and that his conduct was not to be regarded as oppressive towards the minority of shareholders because he individually owned a majority of the stock.

As we have seen in a preceding section, if a majority of the stockholders attempt to manage the affairs of the corporation, not only in their own interest, but in violation of the charter, or in fraud of the rights of the minority, a court of equity will interfere, in a proper case, at the suit of an injured stockholder.¹³⁸

Number of Votes.

In *Taylor v. Griswold*,¹³⁹ it was held that at common law each stockholder of a corporation has but one vote, without regard to the number of shares owned by him, and a by-law allowing one vote for each share was held void. It is generally provided, however, by the charter of joint-stock corporations, or by statute, that stockholders shall have a vote for each share; and this is clearly the just rule, for "stockholders are interested, not equally, but in proportion to the number of shares held by them."¹⁴⁰ Indeed, it has been said that

¹³⁶ *Gamble v. Water Co.*, 123 N. Y. 91, 25 N. E. 201; *North West Transp. Co. v. Beatty*, 12 App. Cas. 589; *Bjorngaard v. Bank*, 49 Minn. 483, 52 N. W. 48.

¹³⁷ 12 App. Cas. 589.

¹³⁸ *Ante*, p. 389.

¹³⁹ 14 N. J. Law, 222, 27 Am. Dec. 33.

¹⁴⁰ 1 Cook, Stock, Stockh. & Corp. Law, § 609.

the custom of giving the shareholders in joint-stock corporations a vote for each share has become so well established that an intention to follow the custom may be implied, in the absence of any indication to the contrary.¹⁴¹ And it has been held, contrary to the decision in *Taylor v. Griswold*, that a by-law giving a vote for each share is valid and binding on all the stockholders.¹⁴² As we have seen, to prevent the corporation from getting into the control of a single person the number of votes which a single stockholder shall be allowed to cast is limited by statute, and the limitation cannot be evaded by transferring the shares to enable the transferees to vote upon them.¹⁴³

Cumulative Voting.

In some states, in order to allow the minority of the stockholders to secure representation on the board of directors, there are statutory or constitutional provisions allowing cumulative voting. Thus, it is provided in West Virginia that, in all elections for directors or managers of corporations, every stockholder shall have the right to vote for the number of shares of stock owned by him for as many persons as there are directors or managers to be elected, or to cumulate said shares, and give one candidate as many votes as the number of directors multiplied by the number of his shares of stock shall equal, or to distribute them, on the same principle, among as many candidates as he shall think fit.¹⁴⁴ The right to cumulative voting does not exist unless expressly given by statute.¹⁴⁵

It has been held that, where the legislature has reserved the right to amend or repeal the charter of a corporation, it may pass an act allowing cumulative voting.¹⁴⁶ This, however, is doubtful; and cer-

¹⁴¹ 1 Mor. Priv. Corp. § 476.

¹⁴² *Com. v. Hemmingway*, 131 Pa. St. 614, 18 Atl. 990, 992.

¹⁴³ Ante, p. 476.

¹⁴⁴ See *Cross v. Railway Co.*, 35 W. Va. 174, 12 S. E. 1071. And see *Wright v. Water Co.*, 67 Cal. 532, 8 Pac. 70; *Horton v. Wilder*, 48 Kan. 222, 29 Pac. 566.

¹⁴⁵ *State v. Stockley*, 45 Ohio St. 304, 13 N. E. 279. In this case it was held that a statute providing that the directors of corporations "shall be chosen, by ballot, by the stockholders who attend for that purpose, either in person, or by lawful proxies; each share shall entitle the owner to as many votes as there are directors to be elected, and a plurality of votes shall be necessary for a choice,"—did not give the right of cumulative voting.

¹⁴⁶ *Cross v. Railway Co.*, 35 W. Va. 174, 12 S. E. 1071.

tainly, if no such power has been reserved, such a statute, as applied to existing corporations, would be unconstitutional, as impairing the contractual rights of the stockholders.¹⁴⁷

Votes by proxy.

The right to vote by proxy must be expressly given, either by a statute or by the charter or by-laws of the corporation, or it does not exist. The common law requires all votes to be given in person.¹⁴⁸ It has been held that, since the common law requires this, a by-law giving the right to vote by proxy is repugnant to law, and therefore void, unless such a by-law is authorized by the charter.¹⁴⁹ By the weight of authority, however, a corporation has the implied power to enact such a by-law.¹⁵⁰ To authorize a vote by proxy, the case must be brought within the terms of the statute, charter, or by-law. Thus, where an act of incorporation provided that each stockholder personally present should be allowed to vote on the stock standing in his name, and that each stockholder, "being a citizen of the United States," might vote by proxy, it was held that an alien stockholder could not vote by proxy.¹⁵¹

A proxy to vote stock can only be given by the legal owner of the stock at the time the vote is to be cast. "The right of voting stock is inseparable from the right of ownership. The one follows as a sequence from the other, and the right to vote cannot be separated from the ownership without the consent of the legal owner."¹⁵² It follows that, where the owner of stock dies, a proxy to vote thereon can only be given by his executors. It cannot be given by the will; nor can a provision in the will that the executors shall give a proxy to a certain person entitle such person to vote the stock, if the executors refuse to give the proxy, for on the death of the owner of stock his ownership ceases, and the executors become the owners.¹⁵³

¹⁴⁷ Ante, pp. 204, 447; *State v. Greer*, 78 Mo. 188.

¹⁴⁸ *Taylor v. Griswold*, 14 N. J. Law, 222, 27 Am. Dec. 83; *Com. v. Bringham*, 103 Pa. St. 184, 49 Am. Rep. 119; *Philips v. Wickham*, 1 Paige, Oh. (N. Y.) 590; *People v. Twaddell*, 18 Hun (N. Y.) 427.

¹⁴⁹ *Taylor v. Griswold*, *supra*.

¹⁵⁰ *Detwiller v. Com.*, 181 Pa. St. 614, 18 Atl. 990; *State v. Tudor*, 5 Day (Conn.) 829, 5 Am. Dec. 162; *People v. Crossley*, 69 Ill 195.

¹⁵¹ *In re Barker*, 6 Wend. (N. Y.) 509.

¹⁵² *Tunis v. Railroad Co.*, 149 Pa. St. 70, 24 Atl. 88.

¹⁵³ *Id.*

A stockholder cannot agree not to give a proxy to vote his shares. Such an agreement is against public policy.¹⁵⁴ In *Fisher v. Bush*,¹⁵⁵ an agreement between a number of stockholders of a corporation that they would not sell or assign their shares, nor give a power of attorney to vote the same, without the consent of all the parties to the agreement, was held void for three reasons; namely, because the agreement not to sell or assign was in restraint of trade, and therefore against public policy; because the agreement not to vote by proxy was pernicious, and contrary to public policy; and because the promises were without consideration.

A power of attorney or proxy to vote stock, though in terms irrevocable, may nevertheless be revoked at any time before the vote, if it is not coupled with an interest.¹⁵⁶ It has often been said, and sometimes held, that such a proxy is not contrary to public policy, but merely revocable.¹⁵⁷ In the late case of *Bostwick v. Chapman* (*Shepaug Voting Trust Cases*),¹⁵⁸ however, it was held contrary to public policy to allow a stockholder to strip himself of the power to vote upon his shares, or to determine how they shall be voted, by giving an irrevocable proxy to one who has no beneficial interest or title in or to the stock or in the affairs of the corporation, and that he can do so neither permanently nor for a term of years. In this case a syndicate owning the majority of the stock of a railroad company had the title put in a trust company to vote for five years according to the direction of a committee, who had no title whatever to the stock. The court held the trust agreement void as against public policy.¹⁵⁹

¹⁵⁴ *Bostwick v. Chapman* (*Shepaug Voting Trust Cases*), 60 Conn. 553, 24 Atl. 32.

¹⁵⁵ 35 Hun (N. Y.) 641.

¹⁵⁶ *Woodruff v. Railroad Co.*, 30 Fed. 91.

¹⁵⁷ See *Brown v. Steamship Co.*, 5 Blatchf. 525, Fed. Cas. No. 2,025.

¹⁵⁸ 60 Conn. 553, 24 Atl. 32.

¹⁵⁹ In speaking of such a power of attorney, Judge Robinson said in *Bostwick v. Chapman*, *supra*: "This I conceive to be against the policy of the law, whether the power so to vote be for five years or for all time. It is the policy of our law that ownership of stock shall control the property and the management of the corporation, and this cannot be accomplished, and this good policy is defeated, if stockholders are permitted to surrender all their discretion and will in the important matter of voting, and suffer themselves to be mere passive instruments in the hands of some agent, who has no interest in the stock, equitable or legal, and no interest in the general prosperity of the corporation. And this is not entirely for the protection of

Stockholders may irrevocably surrender their voting power, and vest it in one who is beneficially interested in the conduct of the business of the corporation, as, for instance, in creditors of the corporation, or in a trustee for creditors, under an agreement for their security.¹⁶⁰

A proxy or power of attorney to vote stock must, of course, be sufficient to show the inspectors that the agent is acting by the authority of the principal, but no peculiar formality is required. It is sufficient if it appears on its face to confer the requisite authority, and is free from all reasonable grounds of suspicion of its genuineness and authenticity.¹⁶¹

Effect of Illegal Reception or Rejection of Votes.

When illegal votes are offered, objection must be raised at the time. If they are not challenged, their receipt will afford no ground for setting the election aside.¹⁶²

Before a stockholder can complain that his vote was not taken at a stockholders' meeting, he must show that he offered to vote, or that he properly presented his claim of right to vote, and that it was excluded.¹⁶³ If the charter and by-laws prescribe no different rule, and the meeting appoints no tellers or inspectors for the purpose, it is for the meeting to determine, in the first instance, the right to vote.

the stockholder himself, but to compel a compliance with the duty which each stockholder owes his fellow stockholder to so use such power and means as the law and his ownership of stock give him that the general interest of stockholders shall be protected, and the general welfare of the corporation sustained, and its business conducted by its agents, managers, and officers, so far as may be, upon prudent and honest business principles, and with just as little temptation to and opportunity for fraud, and the seeking of individual gains at the sacrifice of the general welfare, as is possible. This, I take it, is the duty that one stockholder in a corporation owes to his fellow stockholder; and he cannot be allowed to disburden himself of it in this way. He may shirk it, perhaps, by refusing to attend stockholders' meetings, or by declining to vote when called upon, but the law will not allow him to strip himself of the power to perform his duty. To this extent, at least, a stockholder stands in a fiduciary relation to his fellow stockholders." See *Griffith v. Jewett*, 15 Wkly. Law Bul. 419; *Moses v. Scott*, 84 Ala. 608, 4 South. 742.

¹⁶⁰ *Mobile & O. R. Co. v. Nicholas*, 98 Ala. 92, 12 South. 723.

¹⁶¹ *In re St. Lawrence Steamboat Co.*, 44 N. J. Law, 529.

¹⁶² *In re Election of Directors of Chenango County Mut. Ins. Co.*, 19 Wend. (N. Y.) 635.

¹⁶³ *State v. Chute*, 34 Minn. 135, 24 N. W. 353.

The president of the corporation or chairman of the meeting has no right to pass upon it. And one who, upon an adverse opinion expressed by that officer, refrains from offering his vote, and does not present his claim of right to the meeting for it to pass upon, cannot be heard afterwards to complain.¹⁶⁴

It is not a valid objection to an election that illegal votes were received, or legal votes rejected, unless the majority is thereby changed.¹⁶⁵ And, to set aside an election on such a ground, it must be made to appear affirmatively that the majority is changed. Such a result will not be presumed.¹⁶⁶

Where votes rejected by inspectors at an election of directors, which, if received, would have elected certain candidates, are adjudged to have been erroneously rejected, the only remedy is to set aside the election. The court has no power to declare those candidates elected for whom the votes would have been cast if they had been received.¹⁶⁷ But the court may vacate the seats of directors elected by illegal votes, and declare those elected who received a majority of the legal votes.¹⁶⁸

ELECTION AND APPOINTMENT OF OFFICERS AND AGENTS.

189. Every private corporation has the inherent power to appoint officers and agents to supervise and manage its affairs.

190. No particular formalities are necessary in the appointment of officers and agents, except such as may be prescribed by the charter or by-laws.

A corporation, being impersonal, can only transact its business and make contracts through the intervention of agents. Generally, the

¹⁶⁴ Id.

¹⁶⁵ See *Trustees of School Dist. No. 3 v. Gibbs*, 2 Cush. (Mass.) 39, 45; *Inhabitants of First Parish in Sudbury v. Stearns*, 21 Pick. (Mass.) 148; *Wardens of Christ Church v. Pope*, 8 Gray (Mass.) 140; *Ex parte Murphy*, 7 Cow. (N. Y.) 153; *In re Election of Directors of Chenango County Mut. Ins. Co.*, 19 Wend. (N. Y.) 635; *In re Argus Co.*, 138 N. Y. 557, 34 N. E. 388, 391.

¹⁶⁶ *Ex parte Murphy*, 7 Cow. (N. Y.) 153.

¹⁶⁷ *In re Election of Directors of Long Island R. Co.*, 19 Wend. (N. Y.) 37; *People v. Phillips*, 1 Denio (N. Y.) 388, 396.

¹⁶⁸ *Ex parte Desdoity*, 1 Wend. (N. Y.) 98.

charter of a modern corporation provides what officers and agents shall manage the affairs of the company. Usually, the management is vested in a board of directors, trustees, or managers, who are to be elected periodically by the stockholders. If the charter is silent on the subject, the stockholders may nevertheless elect directors, and invest them with the supervision and management of the corporate affairs, for the power to appoint agents is inherent in all private corporations.¹⁶⁹ A person, in becoming a member of a private corporation, impliedly consents that it shall be represented by such officers and agents as are reasonably necessary for the transaction of its business, and that they shall possess such powers and perform such duties as are ordinarily possessed and performed by such officers and agents.¹⁷⁰

In the appointment of officers and agents of a corporation, no particular formalities are necessary, except in so far as they may be prescribed by the charter or by-laws. A seal is not necessary unless it is so required.¹⁷¹ Nor is a formal vote necessary. "Where one has the actual charge and management of the general business of a corporation, with the knowledge of the members and directors, this is evidence of his authority, without showing any vote or other corporate act constituting him the agent of the corporation."¹⁷² Usually a board of directors is elected by the stockholders, and the directors appoint other officers and agents.¹⁷³ Like a natural person, as we shall see, a corporation may become liable for the acts of a person as its agent by allowing him to appear as having authority to act for it.¹⁷⁴ And it may ratify and render binding acts done without previous authority.¹⁷⁵

¹⁶⁹ Ang. & A. Corp. § 231; Hurlbut v. Marshall, 62 Wis. 590, 22 N. W. 852, 855.

¹⁷⁰ Protection Life Ins. Co. v. Foote, 79 Ill. 361.

¹⁷¹ Bank of Columbia v. Patterson's Adm'r, 7 Cranch, 299, 1 Cumming, Cas. Priv. Corp. 112; Clark, Cont. 282; 1 Mor. Priv. Corp. § 504; ante, p. 157.

¹⁷² Goodwin v. Screw Co., 34 N. H. 378, 1 Cumming, Cas. Priv. Corp. 119. And see Sherman Center Town Co. v. Swigart, 43 Kan. 292, 23 Pac. 569.

¹⁷³ Post, p. 487.

¹⁷⁴ Post, p. 498.

¹⁷⁵ Post, p. 500.

QUALIFICATIONS OF DIRECTORS OR OTHER OFFICERS.

191. No particular qualification is necessary for directors or other officers, unless required by statute, or by the charter or by-laws; but they are generally so expressly required to be stockholders.

Unless required by statute, or by the charter or by-laws of the corporation, a person, to be a director or other officer, need have no particular qualifications. He is generally required to be a stockholder, and, even in the absence of any such requirement, directors are usually chosen by the stockholders from their own number; but there is no rule of law that makes the ownership of stock an indispensable qualification of a director, where there is no such express requirement.¹⁷⁶ Where a director is required to be a stockholder, it has been held sufficient if he holds stock and appears as owner on the books of the corporation, though the share may have been transferred to him merely for the purpose of qualifying him;¹⁷⁷ but this is doubtful, for such a requirement seems clearly to contemplate beneficial ownership of stock by directors.¹⁷⁸

In the absence of express prohibition, a nonresident may be a director; and where directors are required to be stockholders, and nonresidents are not prohibited from owning stock, a nonresident stockholder may be a director.¹⁷⁹ But in some states the directors, or at least a certain number of them, are expressly required to be residents of the state.¹⁸⁰

¹⁷⁶ *Wight v. Railroad Co.*, 117 Mass. 226, 19 Am. Rep. 412. Contra, dictum in *Penobscot R. Co. v. Dummer*, 40 Me. 172, 63 Am. Dec. 654.

¹⁷⁷ *State v. Lute*, 16 Nev. 242.

¹⁷⁸ In *Re Elias* (Sup.) 40 N. Y. Supp. 910, it was held that the New York law providing that "the directors of every stock corporation shall be chosen from the stockholders," and that, "if a director shall cease to be a stockholder, his office shall become vacant," requires the beneficial ownership of stock, as well as the legal title, and that a mere trustee of stock is not eligible for the office of director. And see *Chemical Nat. Bank v. Colwell*, 132 N. Y. 250, 30 N. E. 644.

¹⁷⁹ *Detwiler v. Com.* (Pa. Sup.) 18 Atl. 990.

¹⁸⁰ See *Horton v. Wilder*, 48 Kan. 222, 29 Pac. 586.

In the absence of express provision to the contrary, a director may at the same time hold some other office, as cashier, treasurer, president, etc.¹⁸¹ Indeed, it is generally so.

Persons dealing with a corporation are not bound to inquire into the qualifications of those whom the corporation holds out as its directors. If a corporation elects a person or director who is ineligible to the office, under the by-laws, and permits him to act as such, it will be bound by his acts as director.¹⁸²

POWERS OF DIRECTORS, ETC.

192. Where the general management of a corporation is intrusted to a board of directors or other officers, they have the power to bind the corporation by any act or contract within the powers conferred upon it, except that they cannot effect any great and radical change in the organization of the body, without the assent of the stockholders, unless the power is expressly conferred. The board of directors may delegate an authority to a committee, or to one of their own number, or to third persons, to do acts for the company. And they may ratify acts done without such previous authority. They cannot, however, delegate the exercise of a discretion vested in them.

Where the directors are given the management and control of the corporation, and there are no express limitations on their power, they are competent to make any contract which may be necessary or fit and proper to enable the corporation to accomplish the purposes of its creation. The expediency of making such a contract is committed absolutely to their judgment, and so long as they keep within the power conferred upon the corporation, and act in good faith, with honest motives and for honest ends, their contracts are valid, and conclude the corporation and the stockholders.¹⁸³ Being

¹⁸¹ *Sargent v. Webster*, 13 Metc. (Mass.) 497.

¹⁸² *Despatch Line of Packets v. Bellamy Manuf'g Co.*, 12 N. H. 205.

¹⁸³ *Park v. Locomotive Works*, 40 N. J. Eq. 114, 3 Atl. 162.

invested with the general management of the business of the company, the management and transaction of all business within the powers of the corporation, and the general affairs of the corporation, devolve upon them.¹⁸⁴ Thus, they may make or authorize a valid assignment of the corporate property for the benefit of creditors, where it is in failing circumstances.¹⁸⁵ And they may borrow money, when necessary, and mortgage or convey real estate or personal property of the corporation to pay or secure its debts.¹⁸⁶ And they may assign over securities belonging to the company,¹⁸⁷ or compromise a claim or action pending against it.¹⁸⁸ And they may accept an amendment of the charter authorizing the corporation to take property under the power of eminent domain.¹⁸⁹

As we have seen in a previous section, when the charter of a corporation invests a board of directors or trustees with the power to manage its concerns the power is exclusive, and they alone can act. The stockholders cannot act, nor can they interfere with the directors in their management, or control them otherwise than by electing new directors.¹⁹⁰

It must not be supposed that the powers of the directors are unlimited, for they are not so. They are only invested with the power to manage the affairs of the corporation, and here their authority ends. They have no power to effect any radical change in the organization of the body without the consent of the stockholders. Such powers are impliedly reserved to the stockholders. Thus, where the charter of a corporation empowers it to increase its capital stock, or to make any other fundamental change, but does not pro-

¹⁸⁴ See *Eastern R. Co. v. Boston & M. R. R.*, 111 Mass. 125.

¹⁸⁵ *Wright v. Lee*, 2 S. D. 596, 51 N. W. 706, 714; *Sargent v. Webster*, 13 Metc. (Mass.) 497; *Tripp v. Bank*, 41 Minn. 400, 43 N. W. 60; *Chamberlain v. Bromberg*, 83 Ala. 576, 3 South. 434; *Chase v. Tuttle*, 55 Conn. 455, 12 Atl. 874; *Vanderpoel v. Gorman*, 140 N. Y. 563, 35 N. E. 932; *Wilkinson v. Bauerle*, 41 N. J. Eq. 635, 7 Atl. 514.

¹⁸⁶ *Burrill v. Bank*, 2 Metc. (Mass.) 163, W. D. Smith. Cas. Corp. 112; *Saltmarsh v. Spaulding*, 147 Mass. 224, 17 N. E. 816.

¹⁸⁷ *President, Directors & Company of Northampton Bank v. Pepoon*, 11 Mass. 288.

¹⁸⁸ *Donohoe v. Mining Co.*, 66 Cal. 317, 5 Pac. 495.

¹⁸⁹ *Eastern R. Co. v. Boston & M. R. Co.*, 111 Mass. 125; ante, p. 54.

¹⁹⁰ Ante, p. 447.

vide by whom the power is to be exercised, it cannot be exercised by the board of directors without the assent of the stockholders.¹⁹¹ Nor, on the same principle, can the board of directors wind up the affairs of the company, and dispose of all its property,¹⁹² unless it is insolvent, in which case, as we have seen, they may make an assignment for the benefit of creditors.¹⁹³

The directors can lawfully do no act that is not within the powers conferred upon the corporation by its charter. If they attempt to do so, and, for any reason, relief cannot be obtained through the corporation, a stockholder may maintain a suit to enjoin them.¹⁹⁴

Unauthorized acts or contracts done or entered into by the directors may be ratified by the stockholders, if within the powers of the corporation, and ratification will be implied if they delay for an unreasonable time to take steps to set the transaction aside.¹⁹⁵ Ultra vires acts, of course, cannot be ratified.

Directors de Facto.

Directors de facto, holding office under color of an election, and having charge of the affairs of a corporation, are capable of binding the corporation in all matters legitimately devolving upon directors; and the fact that their election was void and is set aside, and they are removed from office, cannot affect the validity and binding effect of their acts while in office.¹⁹⁶

Appointment of Agents—Ratification.

The board of directors, having general superintendence and active management of the affairs of a corporation, constitute the corporation, to all purposes of dealing with others on its behalf, and do not exercise a delegated authority, in the sense of the maxim, "Delegatus non potest delegare," like agents and attorneys who exercise the powers especially conferred upon them, and no others. Therefore

¹⁹¹ Eldman v. Bowman, 58 Ill. 444; Railway Co. v. Allerton, 18 Wall. 233; Com. v. Cullen, 13 Pa. St. 133.

¹⁹² 1 Mor. Priv. Corp. § 513.

¹⁹³ Ante, p. 486.

¹⁹⁴ Ante, p. 389.

¹⁹⁵ State v. Smith, 48 Vt. 266; Steger v. Davis, 8 Tex. Civ. App. 28, 27 S. W. 1068; Aurora Agricultural & H. Soc., 80 Ill. 263; Reichwald v. Hotel Co., 106 Ill. 439; post, p. 500.

¹⁹⁶ Mining Co. v. Anglo-Californian Bank, 104 U. S. 192.

a board of directors may delegate an authority to a committee, or to one of their own number, or to some other officer, or to outsiders, if they choose, to do acts for the company.¹⁹⁷ Thus, they may authorize a committee of their own number to alienate or mortgage real estate; and such authority necessarily implies an authority to execute suitable and proper instruments for that purpose, and to affix the corporate seal to an instrument requiring it.¹⁹⁸ And the board may authorize one of their number, or some other officer, to assign over any securities belonging to the company which it has the power to assign,¹⁹⁹ or to execute notes for money loaned to the company.²⁰⁰

But the board cannot delegate upon an agent the power to exercise the discretion conferred upon them by the charter. Thus, the power, at discretion, to sell or purchase real property, cannot be delegated, but the board themselves must determine whether to purchase or sell. They can delegate to an agent the power to purchase or sell, after they have determined to do so, but they cannot delegate the power to determine whether the purchase or sale shall be made.²⁰¹

The board may ratify and render valid an act done without previous authority, in any case where they could have authorized it; and they may do so impliedly as well as expressly, as by recognizing the act as binding and acting upon it.²⁰²

DIRECTORS' MEETINGS AND RESOLUTIONS.

193. Where the management of a corporation is vested in a board of directors or trustees, they are the agents of the corporation only when legally acting as a board. They cannot bind the corporation by individual action, but only when regularly assembled at a board meeting.

¹⁹⁷ *Potts v. Wallace*, 146 U. S. 689, 13 Sup. Ct. 196.

¹⁹⁸ *Burrill v. Bank*, 2 Metc. (Mass.) 163; *W. D. Smith, Cas. Corp.* 112.

¹⁹⁹ *President, Directors & Company of Northampton Bank v. Pepoon*, 11 Mass. 288.

²⁰⁰ *Leavitt v. Mining Co.*, 3 Utah, 265, 1 Pac. 356.

²⁰¹ *Bliss v. Irrigation Co.*, 65 Cal. 502, 4 Pac. 507.

²⁰² *Burrill v. Bank*, 2 Metc. (Mass.) 163; *W. D. Smith, Cas. Corp.* 112.

194. The principal rules relating to directors' meetings are these:

- (a) In the absence of express prohibition, directors may meet, and act as agents of the corporation, in another state.**
- (b) Notice of the time and place of the meeting must generally be given each director, unless the meeting is a stated one. But,**
 - (1) If all the directors are present, want of notice is immaterial.**
 - (2) If the charter makes less than all the directors a quorum, with power to transact business, and does not require notice, a quorum may meet and transact business without the presence of, or notice to, the other directors.**
- (c) In the absence of express provision otherwise, a majority of the directors constitute a quorum, and a majority of the quorum may decide any question upon which they may act.**
- (d) A director is disqualified to vote upon any resolution in which he is personally interested.**
- (e) Unless the charter or by-laws so require, the votes and decisions of the directors need not be recorded.**

Directors must Act as a Board.

Where the government of a corporation and management of its affairs are vested in a board of directors (or, as in some states, in a board of trustees), the legal effect is to invest the directors with such government and management as a board, and not otherwise. The general rule is that the governing body, as such, of a corporation, are agents of the corporation only as a board, and not individually. They have authority to act for the corporation only when regularly assembled at a board meeting. The separate action of one or of all of the directors individually is not the action of the body clothed with the corporate powers, and does not bind the corporation.²⁰³

²⁰³ Baldwin v. Canfield, 26 Minn. 43, 1 N. W. 261. In this case a conveyance of land belonging to a corporation was executed in the name of the corporation by

Special Meetings.

Although, by the rules of the corporation, the directors are to have stated meetings, it does not follow that they can have none other. On the contrary, it is a necessary power, incident to the faithful discharge of their trust, that they shall have special or informal meetings when the interests of the corporation require it.²⁰⁴

Place of Meeting.

There is nothing to prevent a corporation from acting by its agents outside of the state by which it was created, if the state in which the acts are done raises no objection. A corporation cannot itself act outside of the state, for it can have no legal existence save in the state to whose laws it owes its existence. They can have no extraterritorial effect.²⁰⁵ It can, however, appoint agents, and they may act for it beyond the limits of the state.²⁰⁶ For most purposes the directors are merely the agents of the corporation, and act as such in the management of its affairs. Therefore, as a general rule, in the absence of express provision to the contrary, they may hold their meetings, and act for the corporation, in another state than

all the directors acting separately, and not as a board, and without any authority from the board. It was held void as a conveyance, and equally ineffectual as a contract to convey. See, also, *In re Marseilles Extension R. Co.*, 7 Ch. App. 161; *D'Arcy v. Railway Co.*, L. R. 2 Exch. 158; *Filon v. Brewing Co.*, 60 Hun, 582, 15 N. Y. Supp. 57; *Schumm v. Seymour*, 24 N. J. Eq. 143; *First Nat. Bank v. Christopher*, 40 N. J. Law, 435; *Gashwiler v. Willis*, 33 Cal. 11; *Junction R. Co v. Reeve*, 15 Ind. 237; *Cammeyer v. United Churches*, 2 Sandf. Ch. (N. Y.) 186; *Stoystown & G. Turnpike R. Co. v. Craver*, 45 Pa. St. 386; *Edgerly v. Emerson*, 23 N. H. 555; *Buttrick v. Railroad Co.*, 62 N. H. 413; *Yellowjacket Silver Min. Co. v. Stevenson*, 5 Nev. 224; *Hillyer v. Mining Co.*, 6 Nev. 51. In Vermont the rule seems otherwise. In *Bank of Middlebury v. Rutland & W. R. Co.*, 30 Vt. 159, it was held that directors could bind their corporation by acting separately, if this was their usual practice in transacting the corporate business. So, in Colorado, where the by-laws of a corporation required claims of officers for compensation to be audited and allowed by the board of directors, it was held a sufficient compliance for a majority of the directors to approve claims, acting separately according to a custom. *Longmont Supply Ditch Co. v. Coffman*, 11 Colo. 551, 19 Pac. 508.

²⁰⁴ *Read v. Gas. Co.*, 9 Heisk. (Tenn.) 545.

²⁰⁵ Ante, p. 77. As to stockholders' meetings, see ante, p. 466.

²⁰⁶ *Bank of Augusta v. Earle*, 13 Pet. 521.

that by which it was created.²⁰⁷ Thus, it has been held that they may meet outside the state, and confer authority upon an agent to execute a deed, mortgage, or other instrument for the corporation,²⁰⁸ or appoint a secretary.²⁰⁹

Notice of Meeting.

To constitute a valid directors' meeting, all of the directors must have notice of the time and place of meeting, unless the meeting is a stated one, so that each one of them is chargeable with notice, or unless a less number than all are made a quorum, and given power to transact business. It is immaterial in what way the day of the regular meetings of directors is fixed. If it has been fixed by usage, a tacit understanding of the members, or in any other way, it is enough.²¹⁰ The purpose of the meeting need not be specified, unless required by the charter or by-laws. When a meeting of directors is notified without specification of the particular purpose, it is to be understood that it is called to consider any matters pertaining to the conduct of the affairs of the corporation that may come before it.²¹¹ It is not necessary that the records of a corporation shall show that all the directors of the corporation had notice of a directors' meeting, or the terms of the notice. In the absence of evidence to the contrary, a sufficient notice will be presumed.²¹² If, by the charter of a corporation, a certain number of directors are made a quorum, and given power to transact business, the corporation is bound by the unanimous concurrence of that number at a casual meeting, and without notice to the others, unless notice is expressly required by the charter or by-laws.²¹³ But in the absence of such a provision a majority of the directors cannot bind the corporation where one of the directors is not present at the consulta-

²⁰⁷ Post, p. 618; *Wright v. Lee*, 2 S. D. 596, 51 N. W. 706, 713.

²⁰⁸ *Arms v. Conant*, 36 Vt. 744; *Bellows v. Todd*, 39 Iowa, 209, 217; *Saltmarsh v. Spaulding*, 147 Mass. 224, 17 N. E. 316.

²⁰⁹ *McCall v. Manufacturing Co.*, 6 Conn. 428.

²¹⁰ *Atlantic Mut. Fire Ins. Co. v. Sanders*, 36 N. H. 252, 269.

²¹¹ *In re Argus Co.*, 138 N. Y. 557, 34 N. E. 388, 394.

²¹² *Sargent v. Webster*, 13 Metc. (Mass.) 497; *Leavitt v. Mining Co.*, 3 Utah, 265, 1 Pac. 356; *Chase v. Tuttle*, 55 Conn. 455, 12 Atl. 874.

²¹³ *Edgerly v. Emerson*, 23 N. H. 555; *State v. Smith*, 48 Vt. 266; *Chase v. Tuttle*, 55 Conn. 455, 12 Atl. 874.

tion, and has not been given notice of the proposed action, and the act is not done at a regular meeting, of which he should know, and at which he might be present.²¹⁴ The fact that notice of a special meeting was not given, even where it was required by the charter or by-laws, is immaterial, if all the directors were present and participated in the proceedings.²¹⁵

“Quorum” and “Majority.”

In the case of a stockholders' meeting, as we have seen, no particular number are required to constitute a quorum, unless there is some charter or statutory provision.²¹⁶ With directors it is otherwise. In the absence of provision to the contrary in a statute, or in the charter or by-laws, a majority of the directors are necessary to constitute a quorum.²¹⁷ A less number cannot act so as to bind the corporation, but can only adjourn. A majority is always enough to constitute a quorum, unless more are expressly required.²¹⁸ It is not necessary that the president of a corporation should be present at a meeting of the directors, in order to authorize them to transact business, unless this is expressly required.²¹⁹

A majority of the quorum have authority to decide any question upon which the board may act.²²⁰ Where the by-laws of a corporation confer upon the directors power to act in behalf of the corporation, without special limitation as to the manner, a majority may act, within the scope of the authority given to the board, and bind the corporation, either where there is a consultation of all together, and a concurrence of a majority, or where there is a regular meeting at which all might be present, and a majority actually attend and act by a major vote.²²¹ And, where the act done at a meeting pur-

²¹⁴ *Despatch Line of Packets v. Bellamy Manuf'g Co.*, 12 N. H. 205.

²¹⁵ *Minneapolis Times Co. v. Nimocks*, 53 Minn. 381, 55 N. W. 546.

²¹⁶ *Ante*, p. 469.

²¹⁷ *Sargent v. Webster*, 13 Metc (Mass.) 497.

²¹⁸ *Sargent v. Webster*, *supra*; *Leavitt v. Mining Co.*, 8 Utah, 265, 1 Pac. 356.

²¹⁹ *Sargent v. Webster*, 13 Metc. (Mass.) 497.

²²⁰ *Sargent v. Webster*, 13 Metc. (Mass.) 497; *Buell v. Buckingham*, 16 Iowa, 284; *Leavitt v. Mining Co.*, 8 Utah, 265, 1 Pac. 356.

²²¹ *Despatch Line of Packets v. Bellamy Manuf'g Co.*, 12 N. H. 205.

ports to be the act of the board, it will be presumed that it was the act of the majority, until the contrary is shown.²²²

As we have just seen, a majority of the directors cannot bind the corporation where one of the directors is not present at the consultation, and has not been given notice of the proposed action, and the act is not done at a regular meeting of which he should know, and at which he might be present.²²³ But where, by the charter of a corporation, a certain number of directors are made a quorum, and given power to transact business, the corporation is bound by the unanimous concurrence of that number at a casual meeting, and without notice to the others, unless notice is expressly required by the charter or by-laws.²²⁴

A director, unlike a stockholder at a stockholders' meeting, is disqualified to vote upon any resolution in which he is personally interested. "All the authorities agree that it is essential that the majority of the quorum of a board of directors shall be disinterested in respect to the matters voted upon."²²⁵

Record of Proceedings.

It is not necessary that the votes or decisions of the directors shall be recorded, unless recording is required by the charter or by-laws. If not recorded, they may be proved by parol. If they are recorded, they must be proved by the record, unless, for some reason, secondary evidence may be admissible.²²⁶

AUTHORITY OF OTHER OFFICERS AND AGENTS.

195. The particular officers and agents of a corporation have such authority only as is expressly conferred upon them by the charter, by-laws, or resolution

²²² *Despatch Line of Packets v. Bellamy Manufg Co.*, 12 N. H. 205; *Heintzelman v. Association*, 38 Minn. 138, 36 N. W. 100.

²²³ *Ante*, p. 491.

²²⁴ *Id.*

²²⁵ *Miner v. Ice Co.*, 98 Mich. 97, 53 N. W. 218; *Smith v. Association*, 78 Cal. 289, 20 Pac. 677; *Copeland v. Manufacturing Co.*, 47 Hun (N. Y.) 235.

²²⁶ *Edgerly v. Emerson*, 23 N. H. 555; *Ten Eyck v. Railroad Co.*, 74 Mich. 226, 41 N. W. 905.

of the board of directors or of the stockholders, and such as is implied because necessary or proper to enable them to perform the duties of their office.

196. If a corporation holds an officer out, or allows him to appear, as having authority not usual to such an office, it will be bound by acts done by him within the scope of his apparent authority.

197. A corporation may ratify any act done without previous authority which it could have authorized. And ratification will be implied from acquiescence, or acceptance of the benefits, with knowledge of the facts.

The powers of the officers of a corporation over its business and property are strictly the powers of agents,—powers either conferred by the charter, or delegated to them by the directors or managers, in whom, as the representatives of the corporation, the control of its business and property is vested. Like the agents of natural persons, they can bind their principal, the corporation, only within the scope of their authority. Their authority, like the authority of agents of natural persons, may be either express or implied. The rules relating to agency generally apply here.

If the general management of the business of a corporation is intrusted to a particular officer by the directors or by the corporation, whatever may be the name given the office,—whether it be “president” or “general manager” or “secretary” or “superintendent,”—such officer has the implied power, in the absence of express limitations, to do all acts on behalf of the corporation that may be necessary or proper in performing his duties; that is, in managing the company’s affairs and conducting its business. Such a general managing officer or agent, for instance, has the implied authority to borrow money on behalf of the corporation, when needed in its business, and to execute its note therefor, and to accept bills or indorse paper in the usual course of the company’s business.²²⁷ So, a person appointed superintendent and manager of a corporation at a

²²⁷ See *Matson v. Alley*, 141 Ill. 284, 31 N. E. 419.

particular place, where the corporation is prosecuting some work, has, in the absence of express limitation, implied authority to purchase supplies and implements, and engage services, necessary or proper for carrying on the work, and may bind the corporation by contracts therefor. His authority extends to all such usual dealings as are necessary to carry on the business from day to day.²²⁸

No officer of a corporation can bind it by any act or contract that is not within the line of his ordinary duties, unless authority is expressly conferred by the charter, or by the stockholders or board of directors. Thus, it has been held that the president and cashier of a bank have no authority, in discounting commercial paper, to agree that the indorser shall not be liable on his indorsement, and such an agreement is not binding on the bank. All discounts being made under the authority of the directors, it is for them to fix any conditions which may be proper in lending money.²²⁹ So, the treasurer, secretary, president, or other officer of a corporation has no implied authority to release a debtor of the corporation from his liability, or to give up securities belonging to the company, without payment. Such power must be expressly given, or it must be implied from a course of dealing known to and sanctioned by the corporation.²³⁰ Such an officer, for instance, cannot release a subscriber from liability on his subscription.²³¹

The powers of the president of a corporation are such only as he derives from the board of directors or other authority to which he owes his appointment. If there is nothing in the charter bestowing special power upon him, he has, from his office merely, no more power over the corporate property and business than any other director.²³² His powers depend upon the authority conferred upon him by the board, and the duties with which he is charged.²³³ Thus,

²²⁸ Rathbun v. Snow, 123 N. Y. 343, 25 N. E. 379.

²²⁹ Bank of United States v. Dunn, 6 Pet. 51.

²³⁰ Moshannon Land & Lumber Co. v. Sloan (Pa. Sup.) 7 Atl. 102.

²³¹ Potts v. Wallace, 146 U. S. 689, 13 Sup. Ct. 196.

²³² Titus v. Railroad Co., 37 N. J. Law, 98; 1 Mor. Priv. Corp. § 537; 2 Cook, Stock, Stockh. & Corp. Law, §§ 712, 716.

²³³ Id.; Walworth County Bank v. Farmers' Loan & Trust Co., 14 Wis. 325; Templin v. Railway Co., 73 Iowa, 548, 35 N. W. 634; Potts v. Wallace, 146 U. S. 689, 13 Sup. Ct. 196.

in the absence of special authority, he cannot dispose of or mortgage the property of the corporation.²³⁴

It is very generally held that the treasurer of a corporation has no implied authority, merely by virtue of his office, to borrow money and execute notes on behalf of the company, or to indorse or transfer securities belonging to the company.²³⁵ Such power must have been expressly conferred by the charter or by-laws, or by resolution of the board of directors, or the directors or managers must have clothed the treasurer with apparent authority.²³⁶ But in Massachusetts it is held that, in the case of a trading or manufacturing corporation, the treasurer is clothed, by virtue of his office alone, with the power to execute notes on behalf of the company;²³⁷ and this rule has in a late case been held to apply to gaslight companies, the business of which requires credit at certain seasons of the year.²³⁸ Even in Massachusetts, however, the rule is held not to extend to a college,²³⁹ nor to a monument association,²⁴⁰ nor to a savings bank,²⁴¹ nor to a horse-railroad company.²⁴² And two of the judges dissented from the decision applying the rule to gaslight companies.²⁴³ The treasurer of a corporation has no implied authority to consent to judgment against the company without suit.²⁴⁴

²³⁴ See cases above cited; and see 2 Cook, Stock, Stockh. & Corp. Law, § 716, and notes, where the cases are collected. See *Leggett v. Banking Co.*, 1 N. J. Eq. 541.

²³⁵ In *re Millward-Cliff Cracker Co.'s Estate*, 161 Pa. St. 157, 28 Atl. 1072; *Craft v. Railroad Co.*, 150 Mass. 207, 22 N. E. 920; *Fifth Ward Sav. Bank v. First Nat. Bank*, 48 N. J. Law, 513, 7 Atl. 318; *Wahlig v. Manufacturing Co.* (City Ct. N. Y.) 9 N. Y. Supp. 739; *First Nat. Bank v. Council Bluffs City Waterworks Co.*, 56 Hun, 412, 9 N. Y. Supp. 859. And see *Chemical Nat. Bank of New York v. Wagner*, 93 Ky. 525, 20 S. W. 535.

²³⁶ As to apparent authority, see post, p. 498.

²³⁷ *Narragansett Bank v. Atlantic Silk Co.*, 3 Metc. (Mass.) 282; *Fay v. Noble*, 12 Cush. (Mass.) 1; *Merchants' Nat. Bank of Gardiner v. Citizens' Gaslight Co.*, 159 Mass. 505, 34 N. E. 1083.

²³⁸ *Merchants' Nat. Bank of Gardiner v. Citizens' Gas Light Co.*, *supra*.

²³⁹ *Webber v. College*, 23 Pick. (Mass.) 302.

²⁴⁰ *Torrey v. Association*, 5 Allen (Mass.) 327.

²⁴¹ *Tappan v. Bank*, 127 Mass. 107.

²⁴² *Craft v. Railroad Co.*, 150 Mass. 207, 22 N. E. 920.

²⁴³ Field, C. J., and Allen, J., dissented.

²⁴⁴ *Stevens v. Iron Co.*, 57 Mich. 427, 24 N. W. 160.

The cashier of a bank, by custom, is its executive officer, through whom the whole financial operations of the bank are conducted. He has implied authority, from his office, without special authority, to transact the ordinary business of the bank, as to receive deposits, and packages of money consigned to the bank; to draw and indorse bills of exchange, checks, and drafts;²⁴⁵ and to certify checks.²⁴⁶ So he has the implied authority to transfer and indorse negotiable notes or bills belonging to the bank,²⁴⁷ or to release a debt secured by mortgage, if he acts in conformity to the rules and practice of the bank.²⁴⁸ But he has no authority, unless it is expressly conferred upon him, to bind the bank by acts and contracts which do not relate to the ordinary business of the bank, or to his ordinary duties as cashier.²⁴⁹ Where discounts, for instance, are made under the authority of the board of directors, and not of the cashier, the cashier can make no special agreement in lending money.²⁵⁰ Nor can a cashier contract with the government, on behalf of the bank, for the transfer of money.²⁵¹ The ordinary duties of cashiers of banks do not comprehend a contract which involves the payment of money, unless it has been loaned in the usual way, nor can a cashier create an agency for the bank, unless he has been expressly authorized to do so.²⁵² Nor can the cashier of a bank execute a mortgage on its property.²⁵³

Persons dealing with a corporation are bound to take notice of its charter, and generally of its by-laws, and if, by these, contracts are required to be made by certain officers or agents only, they cannot hold the corporation liable on a contract made with any other officer or agent. They are bound, at their peril, to ascertain whether the person assuming to contract with the corporation has authority

²⁴⁵ *Merchants' Bank v. Central Bank*, 1 Ga. 418.

²⁴⁶ *Merchants' Bank v. State Bank*, 10 Wall. 604.

²⁴⁷ *Wild v. Bank of Passamaquoddy*, 3 Mason, 505, Fed. Cas. No. 17,646.

²⁴⁸ *Ryan v. Dunlap*, 17 Ill. 40.

²⁴⁹ *Bank of U. S. v. Dunn*, 6 Pet. 51; *U. S. v. City Bank*, 21 How. 356.

²⁵⁰ *Bank of U. S. v. Dunn*, *supra*.

²⁵¹ *U. S. v. City Bank*, *supra*.

²⁵² *Id.*

²⁵³ *Leggett v. Banking Co.*, 1 N. J. Eq. 541.

to bind it.²⁵⁴ This principle is qualified by another, which we shall consider in the following paragraph, namely, that, where a corporation allows another to appear as having authority to bind it in a particular transaction, it will be estopped to deny the apparent authority with which it has clothed him, to the prejudice of persons dealing with him, and cannot even set up a by-law to limit such apparent authority.²⁵⁵

Holding Out—Agency by Estoppel.

It is a well-settled principle of the law of agency that third persons may act upon the apparent authority conferred by the principal upon the agent, and are not bound by secret limitations or instructions qualifying the terms of the written or verbal appointment, and this applies with full force to a corporation which clothes a person with apparent authority to act as its agent.²⁵⁶ An officer of a corporation may, by the acts of its directors or managers, be invested with the capacity to bind the company by his acts beyond those powers which are inherent in and implied from his office. If, in the general course of the company's business, the directors or managers have permitted an officer to assume the direction and control of its affairs, and have held him out to the public as its general agent, his authority to act for the company in a particular transaction may be implied from the manner in which he has been permitted by the directors or managers to transact its business.²⁵⁷ Thus, though the treasurer of a corporation may have no implied authority, by virtue of his office alone, to borrow money and issue negotiable paper therefor on behalf of the corporation, nor to draw or accept bills of exchange or indorse notes, yet, if the directors or other managers allow him to do so, authority will be implied.²⁵⁸

²⁵⁴ *Bocock's Ex'r v. Iron Co.*, 82 Va. 913, 1 S. E. 325.

²⁵⁵ *Post*, pp. 499, 500.

²⁵⁶ *Rathbun v. Snow*, 123 N. Y. 343, 25 N. E. 379; *Marshall v. Express Co.*, 7 Wis. 1, 73 Am. Dec. 381; *Carson City Sav. Bank v. Carson City Elevator Co.*, 90 Mich. 550, 51 N. W. 641; *Sherman Center Town Co. v. Swigart*, 43 Kan. 292, 23 Pac. 569.

²⁵⁷ *Fifth Ward Sav. Bank v. First Nat. Bank*, 48 N. J. Law, 513, 7 Atl. 318; *McNeil v. Boston Chamber of Commerce*, 154 Mass. 277, 28 N. E. 245; *Mining Co. v. Anglo-Californian Bank*, 104 U. S. 192.

²⁵⁸ *Fifth Ward Sav. Bank v. First Nat. Bank*, 48 N. J. Law, 513, 7 Atl. 318;

As we have seen in the preceding paragraph, persons dealing with a person as agent of a corporation are bound to know whether or not he has authority to represent it. This does not mean that they cannot assume that his apparent authority is real, nor that, if a person contracts with an agent acting within the apparent scope of his authority, he is bound, at his peril, to ascertain whether there are any extrinsic facts limiting his authority in the particular transaction. If an officer of a corporation acts within the apparent scope of his authority, persons dealing with him are not bound to have knowledge of extrinsic facts making it improper to act in the particular case.²⁵⁹

By-laws of business corporations are, as to third persons, private regulations, binding as between the corporation and its members, or third persons having knowledge of them; but they are of no force as limitations, per se, as to third persons, of an authority which, except for the by-laws, would be construed as within the apparent scope of the agency. Therefore, where a corporation, for the purpose of mining, among other things, appointed a person "superintendent and manager" at a particular place, it was held that he had apparent authority to purchase, on the credit of the corporation, supplies and implements for carrying on the work, and that the rights of persons contracting with him within such apparent authority could not be affected by a by-law of the corporation, of which they had no notice, providing that no debt should be contracted by any officer or agent of the corporation, nor any obligation created imposing liability upon it, unless expressly authorized by a majority of the board of trustees.²⁶⁰

The fact that an officer of a corporation, like the treasurer, has been in the habit of executing and issuing the notes of the corpora-

Page v. Railroad Co., 31 Fed. 257; Credit Co. v. Howe Mach. Co., 54 Conn. 357, 8 Atl. 472. "The rule is well settled that if a corporation permit the treasurer to act as their general fiscal agent, and hold him out to the public as having the general authority implied from his general name and character, and by their silence and acquiescence suffer him to draw and accept drafts, and to indorse notes payable to the corporation, they are bound by his acts done within the scope of such implied authority." Lester v. Webb, 1 Allen (Mass.) 34.

²⁵⁹ Credit Co. v. Howe Mach. Co., 54 Conn. 357, 8 Atl. 472; New York & N. H. R. Co. v. Schuyler, 34 N. Y. 30, 2 Cumming, Cas. Priv. Corp. 119; post, p. 525.

²⁶⁰ Rathbun v. Snow, 128 N. Y. 343, 25 N. E. 379.

tion, signed by himself alone, without authority, does not abrogate a by-law requiring notes to be countersigned by another officer, or constitute a holding out of such officer as authorized to so issue notes, if neither the directors nor stockholders had knowledge that this was being done.²⁶¹

Where a person has been appointed superintendent of a corporation's business in a foreign country, though by a resolution expressed by word in præsenti, with the understanding both on the part of the corporation and of the appointee that his duties and authority are not to commence until certain preliminary stages of its business shall be completed, he cannot bind the corporation before that time by holding himself out as its active agent to one who relies merely upon his representations, without any knowledge of the resolution.²⁶²

Agency by Ratification.

A corporation, like a natural person, may become bound by the act of a person assuming to act for it without authority, if it ratifies the act. It may ratify, and thereby render binding, any act done without authority which it could have authorized; and an act may be ratified by any officer or board who or which could have authorized it.²⁶³ And ratification may be implied from the conduct of the corporation or its authorized agents, as where it accepts the benefits with notice of the circumstances.²⁶⁴ Thus, if a person, professing to be authorized, mortgages the personal property of a corporation in order to procure a loan, and the money obtained thereby comes into the possession of the corporation, and is retained by it, this will be evidence of a ratification of the mortgage.²⁶⁵

Ratification of an act done by one assuming to act as agent relates back, and is equivalent to a prior authority. When, therefore, the adoption of any particular form or mode is necessary to confer the

²⁶¹ Estate of Millward-Cliff Cracker Co., 161 Pa. St. 157, 28 Atl. 1072.

²⁶² Rathbun v. Snow, 123 N. Y. 343, 25 N. H. 379.

²⁶³ Burrill v. President, etc., 2 Metc. (Mass.) 163, W. D. Smith, Cas. Corp. 112; M'Laughlin v. Railway Co., 8 Mich. 100; Leggett v. Banking Co., 1 N. J. Eq. 541; Aurora Agricultural & Horticultural Soc. v. Paddock, 80 Ill. 263; Reichwald v. Hotel Co., 106 Ill. 439; Grape Sugar & Vinegar Manuf'g Co. v. Small, 40 Md. 395.

²⁶⁴ Cases above cited.

²⁶⁵ Despatch Line of Packets v. Bellamy Manuf'g Co., 12 N. H. 205.

authority in the first instance, there can be no valid ratification, except in the same manner. Thus, if a person executes a contract or conveyance under seal for a corporation, without authority, his act can be ratified only by an instrument under seal, where, as at common law, authority to execute a sealed instrument must be under seal. But parol ratification may render the contract binding as a parol contract, if a seal is not necessary.²⁶⁶

Negotiable Instruments.

Where an officer of a corporation executes and issues negotiable paper, purchasers thereof buy at their peril, as to his authority to execute it; but there is this exception, namely, that if the officer, in issuing the paper, acted within the apparent scope of his authority, but in the particular instance acted wrongfully, and the purchaser had no notice of the wrongful character of the act, or of facts sufficient to put him on inquiry, the purchaser will be protected, as against the corporation.²⁶⁷

Ultra Vires Contracts by Agents.

If a corporation has no power to enter into a particular contract, it cannot, by appointing an agent, become bound by such a contract entered into by him, nor can it become bound by ratification. This is too clear to require argument. "The powers of agents of corporations to enter into contracts in their behalf are limited, by the nature of things, to such contracts as the corporations are by their charters authorized to make. * * * The same want of power to give authority to an agent to contract, and thereby bind the corporation, in matters beyond the scope of their corporate objects, must be equally conclusive against any attempt to ratify such contract. What they cannot do directly they cannot do indirectly. They cannot bind themselves by the ratification of a contract which they had no authority to make. The power of the agent must be restricted to the business which the company was authorized to do.

²⁶⁶ Id.

²⁶⁷ Chemical Nat. Bank v. Wagner, 93 Ky. 525, 20 S. W. 535; Page v. Railroad Co., 31 Fed. 257; Wahlig v. Manufacturing Co. (City Ct. N. Y.) 9 N. Y. Supp. 739; Merchants' Nat. Bank v. Citizens' Gaslight Co., 159 Mass. 505, 34 N. E. 1083; Credit Co. v. Howe Mach. Co., 54 Conn. 357, 8 Atl. 472; Matson v. Alley, 141 Ill. 284, 31 N. E. 419.

Within the scope of the business which they had power to transact, he, as its agent, may be authorized to act for it, but beyond that he could not be authorized, for its powers extend no further.”²⁶⁸

NOTICE TO OFFICER AS NOTICE TO CORPORATION.

198. Knowledge of facts acquired by an officer or agent of a corporation is notice to the corporation, if acquired by him while acting within the scope of his duties, but not otherwise.

It is a well-settled principle of the law of agency that knowledge of facts acquired by an agent is notice to the principal of such facts, if the knowledge is acquired by the agent in the course of his employment, but not otherwise. This principle is applicable to agents of corporations. We have seen that the directors of a corporation represent and have power to bind the corporation only when acting as a board, at a board meeting. It follows that notice to a director, or knowledge derived by him, individually, and not while acting officially, as a member of the board, in the business of the corporation, is not to be regarded, in law, as notice to the corporation.²⁶⁹ In a Connecticut case, after a defective deed had been recorded, purporting to convey certain land, one of the directors of a corporation, not acting as agent of the corporation, and having no management of its business otherwise than as director, went to the town records for the purpose of ascertaining the situation of the land, and there saw the record of the deed; but he did not inform the corporation, or any of its agents, thereof. It was held that the corporation was

²⁶⁸ *Downing v. Road Co.*, 40 N. H. 230, 1 Cumming, Cas. Priv. Corp. 148. Selling railroad bonds upon commission is not within the scope of the corporate powers of a national bank, and therefore no action lies against such a corporation for false representations made by its teller to induce the plaintiff to buy bonds. *Weckler v. Bank*, 42 Md. 581.

²⁶⁹ *Bank of U. S. v. Davis*, 2 Hill (N. Y.) 451; *Buttrick v. Railroad*, 62 N. H. 418; *New Haven, M. & W. R. Co. v. Town of Chatham*, 42 Conn. 465; *Farrell Foundry v. Dart*, 26 Conn. 376; *Farmers' & Citizens' Bank v. Payne*, 25 Conn. 444.

not, by reason of these facts, chargeable with any knowledge of the deed.²⁷⁰ The same principle has often been applied where it was sought to charge a corporation with notice in order to defeat its claim as a bona fide holder of negotiable paper.²⁷¹

This doctrine is by no means limited to directors. It applies to all officers and agents, the only qualification being that the knowledge must be acquired in the course of their employment.²⁷² As was said by the Alabama court in a late case: "Notice to one agent of a corporation with respect to a matter covered by his agency must be as efficacious as to its directors or to its president, since these also are only agents, with larger powers and duties, it is true, but not more fully charged with respect to the particular thing than he whose authority is confined to that one thing."²⁷³ If the officer does not represent the corporation in the transaction by which he acquires knowledge of facts, or where he is acting in his own interest, and against the interest of the corporation,—as where an officer of a corporation procures the corporation to discount a note, of the illegal consideration of which he has knowledge, or where he sells and conveys land to the corporation with knowledge of outstanding eq-

²⁷⁰ *Farrell Foundry v. Dart*, 26 Conn. 376.

²⁷¹ *Farmers' & Citizens' Bank v. Payne*, 25 Conn. 444; and other cases in note 269, *supra*. In this case it appeared that a director of a bank had knowledge of the object for which certain bills of exchange were delivered to a party applying to the bank for a discount thereof, but this director was not present at the meeting of the directors at which such application was made, and the bills discounted; and he did not communicate his knowledge to any other director or officer of the bank. It was held that such knowledge on the part of the director was not notice to the bank.

²⁷² *Saint v. Manufacturing Co.*, 95 Ala. 362, 10 South. 539. Thus, where a defaulting treasurer of a corporation, whose defalcation was as yet unknown, stole money from a third person, and placed it with the funds of the corporation, in order to conceal and make good his defalcation, without the knowledge of any other officer, it was held that the corporation, having used the money as its own, did not thereby acquire a good title to it, as against the true owner, since it was charged with the knowledge of its treasurer, who was its representative in the transaction. *Atlantic Cotton Mills v. Indian Orchard Mills*, 147 Mass. 268, 17 N. E. 496; *Huron Printing & Binding Co. v. Kittleson*, 4 S. D. 520, 57 N. W. 233.

²⁷³ *Saint v. Manufacturing Co.*, 95 Ala. 362, 10 South. 539, 544.

unities,—in which case he could not be supposed to give notice to the corporation, his knowledge cannot be imputed to the corporation.²⁷⁴

CONTRACTS BETWEEN STOCKHOLDER AND CORPORATION.

199. Stockholders or members in a corporation have as much right to contract with it as if they were strangers, and have the same rights under such contracts as a stranger would have.

The members or stockholders, as we have heretofore pointed out, compose the corporation, but they are not the corporation. They have as much right to deal with the corporation as a stranger would have, and may sue it on its contracts. Thus, they may advance money to it in excess of the capital contributed, and the result will be a debt due them by the corporation, which will stand upon exactly the same footing as such a debt due to a stranger.²⁷⁵ And a stockholder who is a creditor of the corporation may be preferred in an assignment made by it in any case where a creditor not connected with the corporation could be preferred.²⁷⁶

RELATION BETWEEN OFFICERS AND CORPORATION.

200. The officers of a corporation, being its agents, and intrusted with the management of its affairs, though not strictly trustees, occupy a fiduciary relation towards it, and cannot, directly or indirectly, derive any personal advantage or profit from their position which is not enjoyed in common by all the

²⁷⁴ *Merchants' Nat. Bank v. Lovitt*, 114 Mo. 519, 21 S. W. 825; *Johnston v. Shortridge*, 93 Mo. 227, 6 S. W. 64; *Frenkel v. Hudson*, 82 Ala. 158, 2 South. 758; *Wickersham v. Zinc Co.*, 18 Kan. 481; *Inverarity v. Bank*, 139 Mass. 332, 1 N. E. 282; *Casco Nat. Bank v. Clark*, 139 N. Y. 307, 34 N. E. 908.

²⁷⁵ See *Lexington Life, Fire & Marine Ins. Co. v. Page*, 17 B. Mon. 412; ante, p. 8. And a stockholder who is a creditor may take a mortgage to secure the debt. *Gordon v. Preston*, 1 Watts (Pa.) 385.

²⁷⁶ *Lexington Life, Fire & Marine Ins. Co. v. Page*, *supra*.

stockholders. Any secret profits made by them in the transaction of the company's business belong to the company.

The cases do not agree in the terms used to designate the relation existing between the directors and other officers of a corporation and the corporation. In most of the cases they are spoken of as "trustees."²⁷⁷ In others they are spoken of as "agents."²⁷⁸ And in others they are termed "mandataries."²⁷⁹ By the better opinion, they are not strictly trustees, but they are simply the agents of the corporation, and they are governed by the rules of law applicable to other agents.²⁸⁰ However much the authorities may disagree in the use of terms to describe the relation, they all agree that the relation is a fiduciary one, and it is generally to express this idea that the relation is spoken of as a "trust relation."

Since the relation between the directors and the corporation is fidu-

²⁷⁷ In *re Cameron's Coalbrook, etc., Ry. Co.*, 18 Beav. 339; *Liquidators of The Imperial Mercantile Credit Ass'n v. Coleman*, L. R. 6 H. L. 189; *Koehler v. Iron Co.*, 2 Black, 721; *Robinson v. Smith*, 3 Paige (N. Y.) 222, 24 Am. Dec. 216; *Shea v. Mabry*, 1 Lea (Tenn.) 319. See note, 53 Am. Dec. 637.

²⁷⁸ *Ferguson v. Wilson*, 2 Ch. App. 77; *Allen v. Curtis*, 26 Conn. 456; *Overend & Gurney Co. v. Gibb*, L. R. 5 H. L. 480.

²⁷⁹ *Spering's Appeal*, 71 Pa. St. 11, 10 Am. Rep. 684.

²⁸⁰ See 1 Mor. Corp. § 516; note, 53 Am. Dec. 637; *Wayne Pike Co. v. Hammons*, 129 Ind. 368, 27 N. E. 487. "The liability of officers to the corporation for damages caused by negligent or unauthorized acts rests upon the common-law rule, which renders every agent liable who violates his authority or neglects his duty to the damage of his principal." *North Hudson Mut. Bld'g & Loan Ass'n v. Childs*, 82 Wis. 460, 52 N. W. 600, 605. "Bank directors are often styled 'trustees,' but not in any technical sense. The relation between the corporation and them is rather that of principal and agent." *Briggs v. Spaulding*, 141 U. S. 132, 11 Sup. Ct. 924, 929. "It is by no means a well-settled point what is the precise relation which directors sustain to stockholders. They are, undoubtedly, said in many authorities to be trustees; but that, as I apprehend, is only in a general sense, as we term an agent or any other bailee intrusted with the care and management of the property of another. It is certain that they are not technical trustees. They can only be regarded as mandataries,—persons who have gratuitously undertaken to perform certain duties, and who are therefore bound to apply ordinary care and diligence, and no more." Per Sharswood, J., in *Spering's Appeal*, 71 Pa. St. 11.

ciary, it follows that a director cannot, directly or indirectly, derive any personal profit or advantage by reason of his position that is not enjoyed in common by all the stockholders.²⁸¹ A director, said the Pennsylvania court in a late case, is a trustee for the entire body of stockholders, and both good morals and good law imperatively demand that he shall manage all the business affairs of the company with a view to promote the common interests, and not his own interests; and he cannot, directly or indirectly, derive any personal profit or advantage, by reason of his position, distinct from the other stockholders. "By assuming the office, he undertakes to give his best judgment, in the interests of the corporation, in all matters in which he acts for it, untrammelled by any hostile interest in himself or others. There is an inherent obligation on his part that he will in no manner use his position to advance his own interest as an individual, as distinguished from that of the corporation. And all secret profits derived by him in any dealings in regard to the corporate enterprise must be accounted for to the corporation, even though the transaction in which they were made also advantaged the corporation of which he was director."²⁸² Thus, where the directors of a corporation secured their own debts by a mortgage of the corporate property, it was held that the mortgage should be set aside.²⁸³ So, where the president of a bank, who was also a director, loaned the moneys of the bank, on a note running to the bank, at a stipulated rate of interest, but on a secret agreement with the borrowers that he should participate in the profits of lands to be purchased with the money, it was held that he was guilty of a breach of trust, and that the profits so acquired by him belonged to the bank.²⁸⁴

²⁸¹ *Arkansas Val. Agr. Soc. v. Eichholtz*, 45 Kan. 164, 25 Pac. 613.

²⁸² *Bird Coal & Iron Co. v. Humes*, 157 Pa. St. 278, 27 Atl. 750; *Koehler v. Iron Co.*, 2 Black, 715; *Farmers' & Merchants' Bank v. Downey*, 53 Cal. 466; *Parker v. Nickerson*, 112 Mass. 195; *Wardell v. Railroad Co.*, 103 U. S. 651; *Cook v. Sherman*, 20 Fed. 167; *Perry v. Cotton-Seed Oil-Mill Co.*, 93 Ala. 364. 9 South. 217; *Flint & P. M. Ry. Co. v. Dewey*, 14 Mich. 477; *Rutland Electric Light Co. v. Bates*, 68 Vt. 579, 35 Atl. 480. Compare *Keeney v. Converse*, 99 Mich. 316, 58 N. W. 325, where stockholders were held barred of relief by reason of laches.

²⁸³ *Koehler v. Iron Co.*, *supra*.

²⁸⁴ *Farmers' & Merchants' Bank v. Downey*, 53 Cal. 466.

This doctrine does not apply where an officer of a corporation enters into a transaction in which he owes no duty to the corporation. It is said by Morawetz that a director or other agent of a corporation may purchase property, and afterwards sell it to the corporation at an advance, provided it was not his duty at the time of the purchase to purchase for the corporation, and that he may purchase claims against the corporation at a discount, and enforce them in full, if he was under no obligation to purchase them for the corporation; and this proposition is abundantly supported by authority.²⁸⁵ If he was under any duty to the company, however, at the time of the purchase, it may claim the benefit of any profit or advantage realized by him. As we shall presently see, at some length, the fiduciary relation in which an officer stands towards the corporation disqualifies him to represent it in making contracts in which he is personally interested. There is much confusion as to the effect of contracts and transactions between a corporation and its officers. Therefore we will reserve the subject for a separate section.

The doctrine of these cases has been applied to a purchase by a director, at an execution sale, of the corporate property, on the ground that it is the duty of a director to prevent such a sale, if possible, and, if not, then to endeavor to have the property produce the highest price, and, in order to the attainment of these objects, to use the knowledge he has derived from the confidence reposed in him as director, while, as purchaser, on the other hand, it is to his interest to pay as little as possible, and to use his special knowledge for his own advantage. And it is held in some states that in such cases actual fraud or actual advantage need not be shown; that the corporation has an absolute right to disaffirm the sale and demand a resale.²⁸⁶ Other courts, however, hold that such a purchase is valid, if in good faith.²⁸⁷

²⁸⁵ 1 Mor. Corp. § 521, and cases there cited. See, also, *St. Louis, Ft. S. & W. R. Co. v. Chenault*, 36 Kan. 51, 12 Pac. 303, where the treasurer of a railroad corporation, who, with his own money, and for himself individually, had purchased notes of the company at a discount, was allowed to collect their full face value from the company, on the ground that, at the time of the purchase, he was under no obligation to purchase or to pay them on behalf of the company.

²⁸⁶ *Hoyle v. Railroad Co.*, 54 N. Y. 595.

²⁸⁷ *Saltmarsh v. Spaulding*, 147 Mass. 224, 17 N. E. 316; *Watt's Appeal*, 78 Pa. St. 370.

CONTRACTS OR OTHER TRANSACTIONS BETWEEN OFFICERS AND THE CORPORATION.

- 201.** An officer cannot, as such, on behalf of the corporation, contract with or convey to himself in his individual capacity, unless he acts under the immediate direction of a superior agent.
- 202.** The directors or other officers of a corporation have no right to represent it in contracts or transactions with themselves, or in which they are personally interested. If they do so, the corporation not being represented by other agents who are disinterested, the contract or transaction is voidable at the option of the corporation. But,
- (a) By the weight of authority, a contract or transaction with an officer, or in which he is personally interested, will be binding upon the corporation if it is shown to be fair and free from fraud, and if the corporation was represented by other agents. In New York and some other jurisdictions it is held, even in these cases, that the contract or transaction may be avoided by the corporation, and that the question of fraud is immaterial.
 - (b) Such a contract or transaction may be ratified by the stockholders, either expressly or impliedly, by acquiescence or acceptance of the benefits with knowledge of the facts.
 - (c) The corporation is liable, on avoiding the contract or transaction, for the benefits actually received and retained.

Contract or Transaction by Officer with Himself.

From the nature of things, the directors or other officers or agents of a corporation cannot contract in their representative capacity with themselves in their capacity as individuals; nor can they convey to themselves. Such a transaction would be void for want of two par-

ties. "The idea," said Orton, J., in a Wisconsin case, "that the same persons constitute different identities of themselves by being called directors or officers of a corporation, so that, as directors or officers, they can convey or mortgage to or contract with themselves as private persons, is in violation of common sense."²⁸⁸ But it has been held that an agent may represent the corporation in making a contract with himself personally, if he acts under immediate instructions from a superior agent, or from the board of directors.²⁸⁹

Personal Interest of Officer in Contract or Transaction.

It is an elementary principle that the same person cannot be allowed to act for himself, and at the same time, with respect to the same matter, as the agent for another, whose interests are conflicting. Thus, a person cannot be a purchaser of property and at the same time the agent of the vendor. "The two positions impose different obligations, and their union would at once raise a conflict between interest and duty; and, constituted as humanity is, in the majority of cases duty would be overborne in the struggle."²⁹⁰ The law therefore will always condemn the transactions of a party on his own behalf, directly or indirectly, when, in respect to the matter concerned, he is the agent of others, and will relieve against them whenever their enforcement is seasonably resisted.²⁹¹ This doctrine applies with full force to transactions by directors or other officers of a corporation, on behalf of the corporation, in which they are personally interested. They will not be permitted to occupy a position in which their own interests will conflict with the interests of the corporation which they represent, and which they are bound to protect. It is well settled, therefore, that, where the directors or other officers or agents of a

²⁸⁸ Haywood v. Lumber Co., 64 Wis. 639, 26 N. W. 184, 187; per Campbell, J., in People v. Township Board of Overysel, 11 Mich. 222; Miner v. Ice Co., 93 Mich. 97, 53 N. W. 218.

²⁸⁹ 1 Mor. Priv. Corp. § 527; Louisville, N. A. & C. Ry. Co. v. Carson, 151 Ill. 444, 38 N. E. 140. In this case a lease to a corporation by a lessor, who also executed the lease on behalf of the company as its vice president and manager, was held good, where it was executed in good faith, under the direction of the president, and ratified by the corporation by taking possession, and paying rent according to its terms.

²⁹⁰ Wardell v. Railroad Co., 108 U. S. 651.

²⁹¹ Id.

corporation are personally interested in any contract or transaction into which they enter on behalf of the corporation, the latter may repudiate it. "They cannot, as agents or trustees, enter into nor authorize contracts on behalf of those for whom they are appointed to act, and then personally participate in the benefits."²⁹² If any profits are made out of such a transaction, they will inure to the benefit of the corporation. Thus, where the directors of a corporation bought a steamboat in their individual capacity, and then, as directors, caused it to be purchased on behalf of the corporation at a large advance upon its cost and value, it was held that the transaction was fraudulent, and that the profits inured to the benefit of the company, and could be recovered by it, with interest.²⁹³ This principle has been applied in a variety of cases. There is no limit to the circumstances under which the question may arise. A director of a corporation is disqualified to vote or act, at a meeting of the board, upon any resolution in which he is personally interested. Thus, he cannot vote on a resolution authorizing the renewal of notes of the corporation in his favor.²⁹⁴ Where the directors fix the compensation for their own services, either as directors or other officers, the transaction will be jealously scrutinized by the courts, and will be set aside, at the election of the corporation, unless it is shown to be fair and free from fraud.²⁹⁵

Extent of Personal Interest.

It can make no difference in the application of this principle that there are other parties to a contract or transaction with a corporation in which an officer is personally interested, who occupy no fiduciary relation to the corporation.²⁹⁶ The doctrine applies, for instance, where a contract is made with a firm of which one of the directors is

²⁹² Id.; *Goodin v. Canal Co.*, 18 Ohio St. 169; *United States Rolling-Stock Co. v. Atlantic & G. W. R. Co.*, 34 Ohio St. 450; *Flint & P. M. R. Co. v. Dewey*, 14 Mich. 477; *Gilman, C. & S. R. Co. v. Kelly*, 77 Ill. 426; *Alling v. Wenzell*, 27 Ill. App. 511; *Gallery v. National Exch. Bank*, 41 Mich. 169, 2 N. W. 193.

²⁹³ *Parker v. Nickerson*, 112 Mass. 195.

²⁹⁴ *Smith v. Association*, 78 Cal. 289, 20 Pac. 677.

²⁹⁵ *Jones v. Morrison*, 31 Minn. 140, 16 N. W. 854. See *Copeland v. Manufacturing Co.*, 47 Hun (N. Y.) 235; *Davis v. Railway Co.*, 22 Fed. 883; *Miner v. Ice Co.*, 93 Mich. 97, 53 N. W. 218.

²⁹⁶ *Munson v. Railway Co.*, 103 N. Y. 58, 8 N. E. 355.

a member,²⁹⁷ or where it is with another corporation of which he is also a stockholder.²⁹⁸ The rule has frequently been applied, for instance, where the directors of a railroad company enter into a contract for the construction of its road with a construction firm or corporation of which one or more of the directors are members.²⁹⁹ So the directors of one corporation cannot act for it in contracting with another corporation, of which they are also directors.³⁰⁰

Where the Corporation is Represented by Other Agents.

Most courts hold that a director or other officer may legally contract with the corporation, if, in entering into the contract, the corporation is represented by other agents; that, for instance, a director, either alone or jointly with strangers, may sell property or lend money to the corporation, or make any other contract with it, if the contract is sanctioned by a majority of the board of directors, not including himself; and that the corporation will be bound if the transaction is fair, open, and free from fraud.³⁰¹ "It cannot be maintained," said Mr. Justice Miller in *Twin-Lick Oil Co. v. Marbury*,³⁰² "that any rule forbids one director among several from lending money to the corporation when the money is needed, and the transaction is open and otherwise free from blame. No adjudged case has gone so far as this.

²⁹⁷ *Aberdeen Ry. Co. v. Blakie*, 1 Macq. 461.

²⁹⁸ *Parker v. Nickerson*, 112 Mass. 195; *Gilman, C. & S. R. Co. v. Kelly*, 77 Ill. 426. And see *Wardell v. Railroad Co.*, 103 U. S. 651.

²⁹⁹ See *Thomas v. Railway Co.*, 2 Fed. 877; *Id.*, 109 U. S. 522, 3 Sup. Ct. 815; *Pearson v. Railroad Corp.*, 62 N. H. 537; *Barr v. Railroad Co.*, 125 N. Y. 263, 26 N. E. 145; *Gilman, C. & S. R. Co. v. Kelly*, 77 Ill. 426.

³⁰⁰ See *United States Rolling-Stock Co. v. Atlantic & G. W. R. Co.*, 34 Ohio St. 450.

³⁰¹ 1 Mor. Priv. Corp. § 527; *Twin-Lick Oil Co. v. Marbury*, 91 U. S. 587; *Barr v. Plate-Glass Co.*, 6 C. C. A. 260, 57 Fed. 86; *Beach v. Miller*, 130 Ill. 162, 22 N. E. 464; *Roseboom v. Whittaker*, 132 Ill. 81, 23 N. E. 339; *Mullanphy Sav. Bank v. Schott*, 135 Ill. 665, 26 N. E. 640; *Louisville, N. A. & C. Ry. Co. v. Carson*, 151 Ill. 444, 38 N. E. 140; *Ten Eyck v. Railroad Co.*, 74 Mich. 226, 41 N. W. 905; *Hallam v. Hotel Co.*, 56 Iowa, 178, 9 N. W. 111; *Garrett v. Plow Co.*, 70 Iowa, 697, 29 N. W. 395; *Buell v. Buckingham & Co.*, 16 Iowa, 284; *Gorder v. Canning Co.*, 36 Neb. 548, 54 N. W. 830; *Parker v. Nickerson*, 137 Mass. 487; *Holt v. Bennett*, 146 Mass. 437, 16 N. E. 5; *Saltmarsh v. Spaulding*, 147 Mass. 224, 17 N. E. 316.

³⁰² 91 U. S. 587.

Such a doctrine, while it would afford little protection to the corporation against actual fraud or oppression, would deprive it of the aid of those most interested in giving aid judiciously, and best qualified to judge of the necessity of that aid, and of the extent to which it may safely be given." Even in such cases as these, however, it is well settled that the transaction will be jealously scrutinized by the courts, and set aside at the instance of the corporation, if the slightest fraud or unfairness appears.³⁰³ And by the better opinion the burden is on the directors or other officers to show the good faith and fairness of the transaction.³⁰⁴

Some of the courts—the New York court among them—have adopted a more rigid rule, and hold that a contract entered into with a corporation, acting through its directors, by one or more of the directors, either alone or jointly with third persons, is voidable at the option of the corporation, though a majority of the directors who assent to the contract are not personally interested, and without regard to whether or not the transaction is fair and free from fraud.³⁰⁵ In these jurisdictions the law does not inquire whether the transaction was fair or unfair, but stops the inquiry as soon as the relation is disclosed, and sets aside the transaction, or refuses to enforce it, at the instance of the corporation, without asking whether there was fraud or not. As was said in a New York case,³⁰⁶ it prevents frauds by making them, as far as may be, impossible, knowing that real motives often elude the most searching inquiry; and it leaves neither to judge nor jury the right to determine, upon a consideration of its advantages or disadvantages, whether a contract made under such circumstances shall stand or fall. It makes no difference in these jurisdictions that only one director is a party to the contract, and

³⁰³ *Thomas v. Railway Co.*, 109 U. S. 522, 3 Sup. Ct. 315; *Twin-Lick Oil Co. v. Marbury*, 91 U. S. 587; *Hallam v. Hotel Co.*, 56 Iowa, 178, 9 N. W. 111; *Hubbard v. Investment Co.*, 14 Fed. 675; *Meeker v. Iron Co.*, 17 Fed. 48.

³⁰⁴ *Wilkinson v. Bauerle*, 41 N. J. Eq. 635, 7 Atl. 514; *Jones v. Morrison*, 31 Minn. 140, 16 N. W. 854.

³⁰⁵ *Aberdeen Ry. Co. v. Blakie*, 1 Macq. 461; *Munson v. Railway Co.*, 103 N. Y. 58, 8 N. E. 355; *Hoyle v. Railroad Co.*, 54 N. Y. 314; *Pearson v. Railroad Corp.*, 62 N. H. 537; *Hoffman Steam Coal Co. v. Cumberland Coal & Iron Co.*, 16 Md. 456.

³⁰⁶ *Munson v. Railway Co.*, 103 N. Y. 58, 8 N. E. 355.

that there were a number of other directors who voted for the contract, and who were not personally interested.

Consent—Acquiescence and Laches of Corporation or Stockholders.

A contract between directors or other officers or agents of a corporation and the corporation, or a transaction with the corporation in which they are interested directly or indirectly, is not absolutely void, even where there is fraud, if it is within the powers of the corporation. It is simply voidable at the election of the corporation or its stockholders.³⁰⁷ To be binding on the corporation, it does not need ratification. It is binding until avoided. It follows that if the stockholders of the corporation, or a majority of them, where the transaction is one which they could have authorized, but not otherwise,³⁰⁸ assent to the contract, expressly or impliedly, by taking the benefit of it with knowledge of the facts, it becomes binding upon the corporation, and cannot afterwards be avoided.³⁰⁹ And such consent will be implied if the stockholders are guilty of laches in moving to avoid it. They must take steps to avoid it within a reasonable time after they have knowledge of the circumstances.³¹⁰ The rule that a contract between a director of a corporation and the corporation is voidable at the instance of the latter, or of its stockholders, clearly does not apply where all who are interested in the corporation, its officers, directors, and stockholders, not only know of but consent to it, and where the property acquired by the cor-

³⁰⁷ *Barr v. New York, L. E. & W. R. Co.*, 125 N. Y. 263, 26 N. E. 145; *Twin-Lick Oil Co. v. Marbury*, 91 U. S. 587; *Hoyle v. Railroad Co.*, 54 N. Y. 314.

³⁰⁸ For instance, the holders of a majority of the stock of a corporation could not, by their votes at a stockholders' meeting, lawfully authorize its officers to lease its property to themselves, or to another corporation formed for the purpose, and whose stock is exclusively owned by them, unless such lease is made in good faith, and is supported by an adequate consideration; otherwise, a fraud would thereby be committed on the minority stockholders. See *Meeker v. Iron Co.*, 17 Fed. 48. As to the powers of the majority, see ante, p. 443.

³⁰⁹ *Barr v. Railroad Co.*, 125 N. Y. 263, 26 N. E. 145; *Louisville, N. A. & O. Ry. Co. v. Carson*, 151 Ill. 444, 38 N. E. 140; *Welch v. Bank*, 122 N. Y. 177, 25 N. E. 269; *Hotel Co. v. Wade*, 97 U. S. 13.

³¹⁰ *Twin-Lick Oil Co. v. Marbury*, 91 U. S. 587; *United States Rolling-Stock Co. v. Atlantic & G. W. R. Co.*, 34 Ohio St. 450. And see *Keeney v. Converse*, 99 Mich. 316, 58 N. W. 325.

poration under the contract is kept and used by it without dissent by any one.⁸¹¹

Liability to Extent of Benefit.

Even where the contract is voidable, and is avoided by the corporation, it will be liable for the actual value of the benefits it has received. Thus, where two of the board of directors of a railroad company, who took part in making a contract for the construction of the road, were interested with the other parties in the contract, and the other contractors entered into an agreement with the other directors at the time the construction contract was made that, in effect, relieved them from liability on their unpaid stock, it was held that the contract was voidable at the election of the corporation or its stockholders, but that, to the extent of the benefit conferred upon the corporation in the construction of the road, the bonds issued in payment thereof were not void, and in a suit to foreclose a mortgage by which they were secured a decree for that amount should be allowed.⁸¹²

LIABILITY OF OFFICERS TO THE CORPORATION.

203. The directors and other officers of a corporation are liable to it for losses sustained

- (a) **By reason of a willful abuse of their trust, as by exceeding their authority or the powers of the corporation, or by misapplication of the corporate funds.**
- (b) **By reason of gross negligence and inattention to the duties of their trust, though there may be no actual bad faith. By the weight of authority, they are bound to exercise ordinary care and prudence,—that is, the same degree of care and prudence that men ordinarily exercise under similar circumstances in their own affairs,—and failure to do so is gross negligence.**

⁸¹¹ *Battelle v. Pavement Co.*, 33 Minn. 89, 33 N. W. 327. And see *Barr v. Glass Co.*, 6 C. C. A. 260, 57 Fed. 86, and *Sanford Fork & Tool Co. v. Howe, Brown & Co.*, 157 U. S. 312, 15 Sup. Ct. 621.

⁸¹² *Thomas v. Railroad Co.*, 109 U. S. 522, 3 Sup. Ct. 315. See, also, *Wardell v. Railroad Co.*, Fed. Cas. No. 17,164.

(c) But they are not liable for accidents, thefts, etc., where they have not been negligent, nor for mere mistakes or errors of judgment, where they have acted in good faith and with ordinary care and diligence.

(d) Nor are they liable for the acts or omissions of other directors or agents, where they have not themselves been guilty of neglect in supervising or appointing them. It is otherwise, however, if they participated in such acts, or negligently failed to take measures to prevent them.

It is well settled that the directors, trustees, or other officers of a corporation, if they act in good faith within the limits of the powers conferred upon the corporation by the charter, and within their authority, and use proper prudence and diligence, are not responsible for losses resulting to the corporation from mere mistakes or errors of judgment.³¹³ Thus, they are not liable for declaring and paying a dividend which diminishes the capital, in violation of a statute or of the common law, where they are not guilty of bad faith or negligence.³¹⁴ Nor are they liable for losses from accident, theft, etc., where they have not been negligent.³¹⁵

On the other hand, all the authorities agree that the directors or other officers of a corporation who willfully abuse their trust, or misapply the funds of the corporation, by which a loss is sustained, are personally liable, as trustees, to make good the loss.³¹⁶ They are bound to observe the limits placed upon their powers in the char-

³¹³ *Spering's Appeal*, 71 Pa. St. 11, 10 Am. Rep. 684, 1 Cumming, Cas. Priv. Corp. 799; *Watts' Appeal*, 78 Pa. St. 370; *Hun v. Cary*, 82 N. Y. 65, 37 Am. Rep. 546; *Hodges v. Screw Co.*, 1 R. I. 312, 53 Am. Dec. 624.

³¹⁴ *Excelsior Petroleum Co. v. Lacey*, 63 N. Y. 422; *Van Dyck v. McQuade*, 86 N. Y. 38; *Lexington & O. R. Co. v. Bridges*, 7 B. Mon. (Ky.) 556.

³¹⁵ *Mowbray v. Antrim*, 123 Ind. 24, 23 N. E. 858.

³¹⁶ *Robinson v. Smith*, 3 Paige (N. Y.) 222, 24 Am. Dec. 212; *Heath v. Railway Co.*, Fed. Cas. No. 6,306; *Perry v. Oil-Mill Co.*, 93 Ala. 364, 9 South. 217; *Ellis v. Ward*, 137 Ill. 509, 25 N. E. 530; *Horn Silver Min. Co. v. Ryan*, 42 Minn. 196, 44 N. W. 56; *Gratz v. Redd*, 4 B. Mon. (Ky.) 178, 195; *Wilkinson v. Bauerle*, 41 N. J. Eq. 635, 7 Atl. 514.

ter and by-laws, and if they intentionally or negligently transcend those powers, and do ultra vires or unauthorized acts, they are liable for the damages.³¹⁷ But they are not liable for violation of the charter through mistake, unless the mistake arose from the want of due care.³¹⁸

And they are equally liable if they suffer the corporate funds or property to be lost or wasted by gross negligence, and inattention to the duties of their trust, though there is no bad faith.³¹⁹ In a late Virginia case it appeared that the president of a savings bank misappropriated its funds and overdrew his accounts, and a brother of the president, and corporations of which the officers and directors were also officers, largely overdrew their accounts, and were loaned large sums by the bank, with little or no security, though such borrowers were irresponsible, and another borrower was permitted to withdraw his security. The directors, though required to meet weekly, met but once, twice, or three times a year, and never caused the books to be examined, nor called for statements of accounts with other banks. The capital of the bank was small, and much of it was not paid up, and the paid-up portion was treated as a loan. The bank, on suspension, was able to pay but 10 per cent. on the deposits. Under these circumstances, it was held that, though the directors were ignorant of the affairs of the bank, and were not guilty of bad faith, they were guilty of such negligence as rendered them liable to the depositors.³²⁰

³¹⁷ *Hun v. Cary*, 82 N. Y. 65, 37 Am. Rep. 546; *Hodges v. Screw Co.*, 1 R. I. 312, 53 Am. Dec. 624.

³¹⁸ *Hodges v. Screw Co.*, *supra*; *Williams v. McDonald*, 37 N. J. Eq. 409; and cases hereafter cited.

³¹⁹ *Robinson v. Smith*, 3 Paige (N. Y.) 222, 24 Am. Dec. 212; *Brinckerhoff v. Bostwick*, 88 N. Y. 52; *Marshall v. Bank*, 85 Va. 676, 8 S. E. 586, 17 Am. St. Rep. 84; *Delano v. Case*, 17 Ill. App. 531, 121 Ill. 247, 12 N. E. 676; *United Society of Shakers v. Underwood*, 9 Bush (Ky.) 609, 15 Am. Rep. 731; *President, etc., of Bank of Mutual Redemption v. Hill*, 56 Me. 385; *Neall v. Hill*, 16 Cal. 145; *Horn Silver Min. Co. v. Ryan*, 42 Minn. 196, 44 N. W. 56; *Gratz v. Redd*, 4 B. Mon. (Ky.) 178, 195; and cases in the following notes.

³²⁰ *Marshall v. Bank*, 85 Va. 676, 8 S. E. 586. Compare *Savings Bank of Louisville's Assignee v. Caperton*, 87 Ky. 306, 8 S. W. 885; *Briggs v. Spaulding*, 141 U. S. 132, 11 Sup. Ct. 924, 2 Cumming, Cas. Priv. Corp. 186, *Shep. Cas. Corp.*

An officer of a corporation is not liable to it for doing *ultra vires* acts, and thereby causing a loss, if the acts were authorized by the corporation; and such authority is shown if it appears that the directors and stockholders knowingly acquiesced therein.³²¹ But the board of directors alone cannot authorize violation of his duty by an officer. Thus, it has been held by the supreme court of the United States that no act or vote of the board of directors of a bank, in violation of their own duties, and in fraud of the interests and rights of the stockholders, will justify the cashier in acts which are in violation of the stipulation in his official bond, well and truly to execute the duties of his office, or exempt him and his sureties from liability thereon.³²²

Officers of a corporation are not bound to exercise the highest degree of care and diligence,—such as a very vigilant or extremely careful person would exercise.³²³ If this were required, it would be difficult to find responsible persons to assume the duties of directors. Nor do they perform their duty by exercising the lowest degree, or slight care, such as inattentive persons would give to their own business. They are bound to exercise ordinary care and prudence,—the same degree of care and prudence that men prompted by self-interest generally exercise in their own affairs. “When,” said the New York court, “one voluntarily takes the position of trustee or director of a corporation, good faith, exact justice, and public policy unite in requiring of him such a degree of care and prudence, and it is a gross breach of duty—‘*crassa negligentia*’—not to bestow them. It is impossible to give the measure of culpable negligence for all

200. In the case last cited, it was held (Harlan, Gray, Brewer, and Brown, JJ., dissenting) that where the affairs of a bank are managed by its president, who has the reputation of being trustworthy and efficient, and owns the greater part of the stock, and the bank is generally considered to be in a prosperous condition, directors cannot be held liable for losses through mismanagement on the ground of negligence, in that they did not, within 90 days after they became directors, compel the board of directors to make a thorough investigation of the books and condition of the bank.

³²¹ *Holmes, Booth & Haydens v. Willard*, 125 N. Y. 75, 25 N. E. 1083.

³²² *Minor v. Bank*, 1 Pet. 46.

³²³ *Briggs v. Spaulding*, *supra*.

cases, as the degree of care required depends upon the subjects to which it is to be applied. What would be slight neglect in the care of a quantity of iron might be gross neglect in the care of a jewel. What would be slight neglect in the care exercised in the affairs of a turnpike corporation, or even of a manufacturing corporation, might be gross neglect in the care exercised in the management of a savings bank."³²⁴ It is generally said that directors and trustees are liable only for gross negligence,—“*crassa negligentia*,”—but, by the weight of opinion, that phrase means the absence of ordinary care and diligence under the circumstances of the particular case.³²⁵ There are some cases against this view of the law,—cases in which it seems to be held that directors will not be liable for losses resulting from their inattention to the duties confided to them unless their inattention was willful or fraudulent.³²⁶ The cases agree that directors cannot be held responsible for the acts or omissions of other directors or agents, unless they have been guilty of neglect in supervising or appointing them.³²⁷

³²⁴ *Hun v. Cary*, 82 N. Y. 65, 71, 37 Am. Rep. 546.

³²⁵ *Hun v. Cary*, *supra*; *Scott v. Depeyster*, 1 Edw. Ch. (N. Y.) 513, 543; *Spering's Appeal*, 71 Pa. St. 11, 10 Am. Rep. 684, 1 Cumming, Cas. Priv. Corp. 799; *Hodges v. Screw Co.*, 1 R. I. 312, 53 Am. Dec. 624; *Marshall v. Bank*, 85 Va. 676, 8 S. E. 586; *Williams v. McKay*, 40 N. J. Eq. 189; *North Hudson Mut. Bldg. & Loan Ass'n v. Childs*, 82 Wis. 460, 52 N. W. 600, 605; *Horn Silver Min. Co. v. Ryan*, 42 Minn. 196, 44 N. W. 56. In *Scott v. Depeyster*, *supra*, it was said: “I think the question in all such cases should and must necessarily be whether they [directors] have omitted that care which men of common prudence take of their own concerns. To require more would be adopting too rigid a rule, and rendering them liable for slight neglect; while to require less would be relaxing too much the obligation which binds them to vigilance and attention in regard to the interests of those confided their care, and expose them to liability for gross neglect only, which is very little short of fraud itself.” In *Spering's Appeal*, *supra*, Judge Sharswood said: “They [directors] can only be regarded as mandataries,—persons who have gratuitously undertaken to perform certain duties, and who are therefore bound to apply ordinary skill and diligence, but no more.”

³²⁶ See *Savings Bank of Louisville's Assignee v. Caperton*, 87 Ky. 306, 8 S. W. 885; *Godbold v. Bank*, 11 Ala. 191; *Neall v. Hill*, 16 Cal. 145.

³²⁷ Directors “are not insurers of the fidelity of the agents whom they have appointed, who are not their agents, but the agents of the corporation; and they cannot be held responsible for losses resulting from the wrongful acts or omissions of

SAME—REMEDIES AGAINST OFFICERS.

204. Where a loss results to a corporation by reason of the fraud, wrong, or negligence of its directors or other agents,

(a) The corporation may maintain

(1) An action on the case at law to recover damages.

(2) A suit in equity to compel them to account.

(b) An individual stockholder in such a case

(1) Cannot maintain an action at law, as the injury is to the corporation.

(2) But he may sue in equity when, and only when, the directors cannot or will not institute the suit, and relief cannot be obtained by applying to a stockholders' meeting.

(c) Creditors of the corporation, in case of insolvency, may enforce the liability to the corporation; and by statute, in a number of states, officers who are guilty of fraud or neglect are expressly made liable to creditors.

205. The statute of limitations does not run against the claim of a corporation against its officers for misappropriation of corporate funds, since their relation is a fiduciary one.

An action on the case by the corporation will lie against the directors or other officers of a corporation for wrongful acts or negligence affecting the interests of the company.³²⁸ And a court of equity, in so far as the individual rights of the stockholders are con-

other directors or agents, unless the loss is a consequence of their own neglect of duty, either for failure to supervise the business with attention, or in neglecting to use proper care in the appointment of agents." *Briggs v. Spaulding*, 141 U. S. 132, 11 Sup. Ct. 924, 929, 2 Cumming, Cas. Priv. Corp. 186; *Shep. Cas. Corp.* 200.

³²⁸ *Franklin Fire Ins. Co. v. Jenkins*, 3 Wend. (N. Y.) 130; *Horn Silver Min. Co. v. Ryan*, 42 Minn. 196, 44 N. W. 56.

cerned, has jurisdiction to call the directors to account for breach of trust, and to compel them to make satisfaction to the corporation for any loss sustained by it.³²⁹ Such a suit should ordinarily be brought by the corporation, for the injury is to it, and not by individual stockholders. But a stockholder, as we have seen, may maintain a suit in equity for the benefit of the corporation, where the directors cannot or will not institute the suit in the name of the corporation, and relief cannot be obtained by applying to a stockholders' meeting.³³⁰ An individual stockholder cannot maintain an action at law against the directors or other officers of the corporation for fraud or negligence resulting in loss of corporate property. There is, in the eye of the law, no privity or relation between the stockholders and directors. The directors are not the agents of the stockholders, but of the corporation, the legal entity; and therefore, at law, the corporation alone can sue for injuries to it.³³¹ If a corporation becomes insolvent, creditors may enforce in equity a liability of its officers to the corporation for fraud or neglect resulting in loss to the corporation.³³² In most states corporate officers are by statute expressly made liable to creditors of the corporation for certain delinquencies in the performance of their duties.³³³

Statute of Limitations.

The statute of limitations does not run against the claim of a corporation against its officers for misappropriation of corporate funds, since their relation to such funds is fiduciary.³³⁴

³²⁹ Robinson v. Smith, 3 Paige (N. Y.) 222, 24 Am. Dec. 212; Brinckerhoff v. Bostwick, 88 N. Y. 52; Hodges v. Screw Co., 1 R. I. 312, 53 Am. Dec. 624.

³³⁰ Robinson v. Smith, 3 Paige (N. Y.) 222, 24 Am. Dec. 212; Horn Silver Min. Co. v. Ryan, 42 Minn. 196, 44 N. W. 56; Greaves v. Gouge, 69 N. Y. 154; Brinckerhoff v. Bostwick, 88 N. Y. 52; Hodges v. Screw Co., 1 R. I. 312, 53 Am. Dec. 624; Heath v. Railway Co., 8 Blatchf. 347, Fed. Cas. No. 6,306; Hersey v. Veazie, 24 Me. 9; Mussina v. Goldthwaite, 34 Tex. 125; Wayne Pike Co. v. Hammons, 129 Ind. 368, 27 N. E. 487.

³³¹ Smith v. Hurd, 12 Metc. (Mass.) 371, 46 Am. Dec. 690.

³³² Post, p. 605.

³³³ Post, p. 609.

³³⁴ Ellis v. Ward, 137 Ill. 509, 25 N. E. 530.

LIABILITY OF OFFICERS AND AGENTS ON CONTRACTS.

206. The liability of officers and agents upon contracts made by them on behalf of the corporation, both where they have authority, and where they have no authority at all, or exceed their authority, is the same as if they were contracting for a natural person.

The liability of officers and agents of a corporation on contracts entered into by them is the same as in the case of any other person assuming to act as agent for another. The questions that arise in this connection are not at all peculiar to the law of corporations, but depend entirely upon established principles of the law of agency. An agent of a corporation may enter into a contract without disclosing the fact that he is acting for the corporation. His liability in such a case is precisely the same as if he acted for an undisclosed natural principal. For the law on this subject, therefore, reference must be had to works on the law of agency.³³⁵

So where an officer or agent of a corporation enters into a contract for the corporation in excess of his authority, or where a person enters into a contract for a corporation without any authority at all, his liability is the same as if he were acting for a natural person,—neither greater nor less. It will be found, upon consulting the law of agency, which is applicable in this connection to corporations, that if a person contracts as agent on behalf of a principal who does not exist, or who cannot contract, or if he enters into a contract in excess of his authority, he is personally liable, in some form of action, to the other party. Whether he is liable *ex contractu*, or whether he is liable only in tort, is an unsettled question, and there is a conflict of opinion. Some of the courts hold that the agent in such a case is liable in contract if he acted in good faith, and in tort if he acted in bad faith. If he believed that he had authority which he did not have, he may be sued as upon an implied warranty of au-

³³⁵ See Clark, *Cont.* 740, 742.

thority. This rule has often been applied to contracts by persons contracting for a corporation without authority, or in excess of authority.³³⁶ Thus, where the president of a corporation executed a written guaranty in the name of the company, but without authority, he was held individually liable on the guaranty, as upon an implied warranty of authority.³³⁷ So where a person, assuming to represent a foreign corporation doing business in a state without compliance with the statute prescribing the conditions upon which foreign corporations may do business, engaged the services of a person and purchased goods for the corporation, he was held personally liable therefor.³³⁸

Some courts have refused to recognize this doctrine of implied warranty of authority, and hold that the liability of an agent acting without authority, or in excess of authority, is in tort, whether he acted in bad faith or not. In these jurisdictions a person who assumes to contract for a corporation without authority, or in excess of authority, is personally liable, whether he acted in bad faith or not, but he is liable only in an action of tort.³³⁹ "If one falsely represents that he has an authority, by which another, relying on the representation, is misled, he is liable; and by acting as agent for another when he is not, though he thinks he is, he tacitly and impliedly represents himself authorized, without knowing the fact to be true, it is in the nature of a false warranty, and he is liable. But in both cases his liability is founded on the ground of deceit, and the remedy is by action of tort."³⁴⁰ On this subject the reader must refer to works on the law of agency.

³³⁶ *Farmers' Co-op. Trust Co. v. Floyd*, 47 Ohio St. 525, 28 N. E. 110; *Nelligan v. Campbell*, 20 N. Y. Supp. 234; *Lasher v. Stimson*, 145 Pa. St. 30, 23 Atl. 552; *Lewis v. Tilton*, 64 Iowa, 220, 19 N. W. 911.

³³⁷ *Nelligan v. Campbell*, 65 Hun, 622, 20 N. Y. Supp. 234.

³³⁸ *Lasher v. Stimson*, 145 Pa. St. 30, 23 Atl. 552.

³³⁹ *Jefts v. York*, 10 Cush. (Mass.) 392; *Farmers' & Mechanics' Bank v. Colby*, 64 Cal. 352, 28 Pac. 118.

³⁴⁰ *Jefts v. York*, *supra*.

**LIABILITY OF CORPORATION FOR TORTS OF OFFICERS
AND AGENTS.**

207. A corporation is generally liable for the torts of its officers and agents committed in the course of their employment, to the same extent as a natural person. There are some exceptions, resulting from the peculiar nature of a corporation.

208. A corporation is liable for acts done by its officer or agent apparently in the course of his employment, and within the scope of his general authority, though, by reason of facts peculiarly within the knowledge of the officer or agent, the particular act is unauthorized.

209. As to whether a corporation is liable for torts committed by its agents in the performance of ultra vires acts, the courts do not agree. By the weight of authority, it is liable in such a case if it authorized the ultra vires acts, but not otherwise.

We have seen in a previous chapter that a corporation can be guilty of a tort, and have shown the exceptions to the rule resulting from the peculiar nature of the corporation as an artificial being.³⁴¹ Of course, a corporation, being impersonal, cannot personally commit a tort. It can act only through agents, but, like a natural person, it is liable for the torts of its agents. The general rule is that a corporation is liable for the wrongful acts of its officers and agents to the same extent, and only to the same extent, as a natural person is liable for the wrongful acts of his agents. Most of the rules and principles are the same in both cases. If a corporation expressly authorizes a person to do a particular act, there would seem to be no question as to its liability. Thus, if a majority of the stockholders should, by vote, direct an agent to enter unlawfully upon the land

³⁴¹ Ante. p. 193.

of another, the corporation would clearly be liable in trespass. The difficulties arise in those cases where the authority of the agent is to be implied.

It is the general rule that a corporation, like a natural person, is liable for any act of its agent that is committed in the conduct of its business, and in the course of his employment. "A principal," said Mr. Justice Story, "is to be held liable to third persons, in a civil suit, for the frauds, deceits, concealments, misrepresentations, negligences, and other malfeasances or misfeasances and omissions of duty of his agent in the course of his employment, although the principal did not authorize or justify or participate in, or, indeed, know of, such misconduct, or even if he forbade the acts, or disapproved of them. In all such cases the rule applies, respondeat superior, and is founded upon public policy and convenience; for in no other way could there be any safety to third persons in their dealings, either directly with the principal, or indirectly with him, through the instrumentality of agents. In every such case the principal holds out his agent as competent and fit to be trusted, and thereby, in effect, he warrants his fidelity and good conduct in all matters within the scope of the agency."³⁴² This statement of the rule applies to officers and agents of corporations.³⁴³

Some of the cases are very clear. For example, if an agent having authority to sell goods for a corporation should be guilty of false and fraudulent representations as to their quality, the corporation is clearly liable to an action for deceit. The fraud in such a case is, for all purposes, the fraud of the corporation, though it may not have authorized it, since it is committed by the agent in the course of his employment; that is, in selling goods.³⁴⁴ And so, generally, a corporation is liable for all frauds of its agents com-

³⁴² Story, Ag. § 452.

³⁴³ Fifth Ave. Bank of New York v. Forty-Second St. & Grand St. Ferry R. Co., 137 N. Y. 231, 33 N. E. 378; Philadelphia, W. & B. R. Co. v. Quigley, 21 How. 207, 1 Cumming, Cas. Priv. Corp. 453; Denver & R. G. Ry. v. Harris, 122 U. S. 597, 7 Sup. Ct. 1286; Salt Lake City v. Hollister, 118 U. S. 256, 6 Sup. Ct. 1055, 2 Cumming, Cas. Priv. Corp. 107; State v. Morris & E. R. Co., 23 N. J. Law. 369.

³⁴⁴ Ante, p. 196. See 8 Am. Law Rev. 631.

mitted in the course of their employment.³⁴⁵ And, as we have seen in a former chapter, a corporation is liable for assault and battery, or other trespasses, for conversion, for libel, for malicious prosecution, or malicious attachment of goods, or for conspiracy, or for negligence, by or of its officers or agents, if committed in the course of their employment.³⁴⁶

The fact that an officer or agent acts without the scope of his actual authority, in committing a fraud, does not exempt the corporation from liability, if his act was apparently done in the course of his employment, and within the scope of the general authority conferred upon him. If an act is apparently within the scope of the general authority and employment of the agent, though, by reason of facts necessarily and peculiarly within his knowledge, it is unauthorized, the corporation is liable. Thus, where the secretary and treasurer of a corporation, who was also its agent for the transfer of stock and authorized to countersign and issue certificates of stock when signed by the president, forged the president's name to a certificate, and fraudulently issued it, the corporation was held liable to a bank which accepted the certificate, in good faith, as security for a loan; and there are many other cases to substantially the same effect.³⁴⁷

³⁴⁵ *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 2 Cumming, Cas. Priv. Corp. 119; note 347, *infra*. It is liable for the fraud of agents in procuring subscriptions to its stock. *Ante*, p. 283.

³⁴⁶ *Ante*, pp. 194-196, and cases there cited.

³⁴⁷ *Fifth Ave. Bank of New York v. Forty-Second St. & Grand St. Ferry R. Co.*, 137 N. Y. 231, 33 N. E. 378, 2 Cumming, Cas. Priv. Corp. 149. It was said in this case: "It is true that the secretary and transfer agent had no authority to issue a certificate of stock except upon the surrender and cancellation of a previously existing valid certificate, and the signature of the president and treasurer first obtained to the certificate to be issued; but these were facts necessarily and peculiarly within the knowledge of the secretary, and the issue of the certificate in due form was a representation by the secretary and transfer agent that these conditions had been complied with, and that the facts existed upon which his right to act depended. It was a certificate apparently made in the course of his employment, as the agent of the company, and within the scope of the general authority conferred upon him; and the defendant is under an implied obligation to make in-

If the transaction in which an officer or agent of a corporation commits a fraud is not even apparently within the scope of his authority, the corporation is not liable.³⁴⁸ If the agent of a corporation goes outside of his employment, he does not act as agent, and the corporation cannot be held liable. Thus, it has been held that a street-railway company is not liable for a malicious prosecution and false arrest of an individual by its president and superintendent on the charge of having passed counterfeit money by dropping a lead nickel in the fare box, unless such officers have express authority for such action, or it is ratified by the company.³⁴⁹ And clearly a corporation cannot be held liable for the fraud of its president, who, in negotiating for a loan to himself individually, falsely represents that certificates of stock in the corporation, which he offers as collateral, are genuine.³⁵⁰ So, where a corporation delivers to the manager of its business surrendered certificates of stock containing blank indorsements, with directions to cancel them, and he transfers them to a purchaser in good faith, the title of the purchaser cannot be upheld, as against the corporation, on the ground of any implied agency on the part of the manager to transfer them. As was said in such a case: "If it can be said that the direction of the president to the manager to cancel the certificates made him the agent of the company for that purpose, it was an authority to destroy, and not to use. His act in abstracting

demnity to the plaintiff for the loss sustained by the negligent or wrongful exercise by its officers of the general powers conferred upon them." See, also, *Griswold v. Haven*, 25 N. Y. 599; *New York & N. H. R. Co. v. Schuyler*, 34 N. Y. 30, 2 Cumming, Cas. Priv. Corp. 119; *Titus v. Turnpike Road*, 61 N. Y. 237; *Bank of Batavia v. New York, L. E. & W. R. Co.*, 106 N. Y. 199, 12 N. E. 433; *Manhattan Beach Co. v. Harned*, 27 Fed. 484; *Tome v. Railroad Co.*, 39 Md. 36; *Shaw v. Mining Co.*, 13 Q. B. Div. 103; *Allen v. Railroad Co.*, 150 Mass. 200, 22 N. E. 917. Cf. *Moore v. Bank*, 111 U. S. 156, 4 Sup. Ct. 345, 2 Cumming, Cas. Priv. Corp. 144; ante, p. 438, note 115; *Farrington v. Railroad Co.*, 150 Mass. 406, 23 N. E. 109; *Hill v. Publishing Co.*, 154 Mass. 172, 28 N. E. 142.

³⁴⁸ *Weckler v. Bank*, 42 Md. 581, 2 Cumming, Cas. Priv. Corp. 104; *Shep. Cas. Corp.* 150.

³⁴⁹ *Central Ry. Co. v. Brewer*, 78 Md. 394, 28 Atl. 615.

³⁵⁰ *Manhattan Life Ins. Co. v. Forty-Second St. & G. St. Ferry R. Co.*, 64 Hun, 635, 19 N. Y. Supp. 90, affirmed 139 N. Y. 146, 34 N. E. 776; *Moore v. Bank*, 111 U. S. 156, 4 Sup. Ct. 345, 2 Cumming, Cas. Priv. Corp. 144.

them from the safe, and uttering them as valid certificates, had no relation to the authority conferred. It was not an act of the same kind as that which he was authorized to perform. He had no apparent authority to issue them as genuine certificates, for he had no authority to issue certificates for any purpose; and what he did was a willful and criminal act, perpetrated for private gain, and not connected with any official authority or semblance of authority, which he possessed as the defendant's agent."³⁵¹ If the tort is committed by the agent in the course of his employment, the corporation cannot escape liability on the ground that it was not authorized, or even that it was expressly forbidden, and it can make no difference that the agent acts willfully and maliciously.³⁵² This rule is not peculiar to corporations. It is a well-settled principle of the general law of agency.³⁵³ Thus, a railroad company has repeatedly been held liable for the act of its conductor in assaulting a passenger, and the rule has been applied to other employes.³⁵⁴ A railroad company has been held liable to a woman passenger for the tortious conduct of the conductor in kissing her.³⁵⁵

Ratification.

A corporation, like a natural principal, may become liable for torts of a person assuming to act for it, by ratifying his act, though the act was not authorized when it was committed. It will become liable by ratification if the act was done to its use or for its benefit, but not otherwise.³⁵⁶ "He that receiveth a trespasser, and agreeth to a trespass after it be done, is no trespasser, unless the trespass was done to his use or for his benefit, and then his subsequent agreement amount-

³⁵¹ Knox v. American Co., 148 N. Y. 441, 42 N. E. 988.

³⁵² Wheeler & W. Manuf'g Co. v. Boyce, 36 Kan. 350, 13 Pac. 609.

³⁵³ See Tiff. Pers. & Dom. Rel. 505-507, and works on Agency, and on Torts.

³⁵⁴ Passenger R. Co. v. Young, 21 Ohio St. 518; Bryant v. Rich, 106 Mass. 180; Rounds v. Railroad Co., 64 N. Y. 129; Dwinelle v. Railroad Co., 120 N. Y. 117, 24 N. E. 319; Chicago & E. R. Co. v. Flexman, 103 Ill. 546; North Chicago City Ry. Co. v. Gastka, 128 Ill. 613, 21 N. E. 522.

³⁵⁵ Croker v. Railway Co., 36 Wis. 657.

³⁵⁶ Eastern Counties Ry. Co. v. Broom, 6 Exch. 314, 1 Cumming, Cas. Priv. Corp. 434; Nims v. School, 160 Mass. 177, 35 N. E. 776.

eth to a commandment.”³⁵⁷ If the servant of a railroad company arrests and imprisons a passenger without authority, for nonpayment of his fare, his act is one which might be for the benefit of the company; and, if the company subsequently ratifies the act, it is liable in tort, should the act prove to have been unlawful.³⁵⁸

Ultra Vires Transactions.

There is a wide difference of opinion, and much conflict and confusion in the decisions, as to the liability of a corporation for torts committed by its officers or agents in the performance of ultra vires acts, or in the course of ultra vires transactions. Some of the authorities hold, or seem to hold, broadly, that a corporation is not liable for the tortious conduct of its officers or agents in the course of an ultra vires transaction, as it cannot authorize ultra vires acts. Thus, where the officers of an agricultural society authorized to hold agricultural fairs employed certain persons to convey persons to and from the fair grounds, and one of these persons negligently injured a third person, it was held that the corporation was not liable, as the employment was not within the powers of the corporation.³⁵⁹ So where the teller of a national bank, acting for it in selling railroad bonds, made false representations to induce a person to buy the bonds, it was held that the bank was not liable, as the sale of railroad bonds was not within the corporate powers of national banks.³⁶⁰ There are many other cases in which the same principle is laid down.³⁶¹

Many of these cases can be supported on the ground that the transaction was not authorized by the corporation, and that the tort, therefore, was not committed by the officer or agent within the scope of his employment. Thus, if, in the case above referred to, the officers of the agricultural society were not authorized by the corporation to employ persons to convey people to and from the fair

³⁵⁷ 4 Inst. 317.

³⁵⁸ Eastern Counties Ry. Co. v. Broom, *supra*.

³⁵⁹ Bathe v. Society, 73 Iowa, 11, 34 N. W. 484.

³⁶⁰ Weckler v. Bank, 42 Md. 581, 2 Cumming, Cas. Priv. Corp. 104, Shep. Cas. Corp. 150.

³⁶¹ Gunn v. Railroad Co., 74 Ga. 509, 2 Cumming, Cas. Priv. Corp. 111.

grounds, they exceeded their authority in doing so, and for this reason, and not because the transaction was ultra vires of the corporation, the corporation could not be held liable. So, in the national bank case above referred to, the decision may be based on the ground that the teller, in selling the railroad bonds, did not act within the scope of his employment. By the weight of authority, the principle does not go beyond this. And most of the courts hold that if a corporation, as distinguished from the officers and agents of the corporation, engages in an ultra vires transaction, it will be liable for the frauds, negligence, or other torts of its agents in the course of that transaction; that a corporation has the power or capacity, as distinguished from the authority or right, to do ultra vires acts and to engage in ultra vires transactions; and that, if it does so, it cannot escape liability for torts committed in the course of such transactions merely on the plea of ultra vires. The question always narrows itself to this: Did the corporation authorize the transaction, either expressly or impliedly? If it did, it is liable. Thus, where an educational corporation maintained a ferry, it was held liable for injuries to a passenger while being transported thereon, though the maintenance of the ferry by such a corporation was clearly ultra vires.³⁶² So, where railroad companies were operating their roads jointly under an ultra vires agreement, they were held liable for injuries to a passenger.³⁶³ And a railroad company was held liable for the negligence of the driver of a stage-coach which it was running without the right to engage in business of that kind.³⁶⁴ So, where a bank which was accustomed to take deposits of United States bonds, with the knowledge and acquiescence of its directors, took such a deposit, and the bonds were lost through the gross carelessness of its agents, it was held liable for the loss,

³⁶² *Nims v. School*, 160 Mass. 177 35 N. E. 776.

³⁶³ *Bissell v. Railroad Co.*, 22 N. Y. 258, 1 Cumming, Cas. Priv. Corp. 187.

³⁶⁴ *Buffett v. Railroad Co.*, 40 N. Y. 168. And see, to substantially the same effect, *Central Railroad & Banking Co. v. Smith*, 76 Ala. 572; *New York, L. E. & W. Ry. Co. v. Haring*, 47 N. J. Law, 137, 2 Cumming, Cas. Priv. Corp. 110; *Hutchinson v. Railroad Co.*, 6 Heisk. (Tenn.) 634. See, contra, cases in notes 359-361, *supra*.

to the same extent as if the taking of the deposit had been authorized by its charter. Corporations, it was said, are liable for every wrong they commit, and in such cases the doctrine of ultra vires has no application.³⁶⁵ Many other cases to the same effect may be found.³⁶⁶

LIABILITY OF OFFICERS AND AGENTS TO THIRD PERSONS FOR TORTS.

210. If the officers of a corporation, in transacting its business, are guilty of false and fraudulent representations, or other torts, whereby third persons are injured, they are personally liable.

It is well settled that, if the directors or other officers of a corporation commit frauds upon third persons in their transactions as officers of the company, they are personally liable to an action therefor, though the corporation also may be liable. Their liability does not depend upon their agency for the corporation. They are liable simply because they have been guilty of a tort. Thus, the directors of a corporation are personally liable to a third person for fraudulent representations whereby he was induced to contract with the corporation to his injury. There is no privity of contract between them and such person, but that can make no difference, for the action is not founded upon the contract at all, nor upon a breach thereof, but upon the personal tort of the directors.³⁶⁷ So a director or other officer of a corporation who knowingly issues or sanctions a false report or prospectus, containing untrue statements of material facts, the natural tendency of which is to mislead and deceive the community, and to induce the public to purchase stock of the corporation, or to deal with it,

³⁶⁵ *National Bank v. Graham*, 100 U. S. 699.

³⁶⁶ See *Salt Lake City v. Hollister*, 118 U. S. 256, 6 Sup. Ct. 1055, 2 Cumming, Cas. Priv. Corp. 107; *Denver & R. G. Ry. Co. v. Harris*, 122 U. S. 597, 7 Sup. Ct. 1286; *Id.*, 2 Pac. 369.

³⁶⁷ *Salmon v. Richardson*, 30 Conn. 360; *Cowley v. Smyth*, 46 N. J. Law, 380; *Clark v. Edgar*, 84 Mo. 106; *Schley v. Dixon*, 24 Ga. 273; *Zinn v. Mendel*, 9 W. Va. 580.

is personally liable, in an action of deceit, to persons who purchase stock or deal with the corporation in reliance thereon, and are defrauded.⁸⁶⁸

To render the officers of a corporation liable to third persons for fraud, the case must come within the rules governing other cases of false representations. Therefore the representation must have been false. It must also have been fraudulent; that is, they must have known it to be false, or must have made it willfully, or in reckless disregard of whether it was true or false.⁸⁶⁹ The person seeking to hold them liable must have relied on the representation,⁸⁷⁰ and must have sustained injury in consequence thereof.⁸⁷¹

To render an officer or member of a corporation personally liable for torts committed in the conduct of its business, he must have personally taken part in the act, or knowingly acquiesced in it, when it was his duty to object and take steps to prevent it.⁸⁷²

COMPENSATION OF OFFICERS.

211. An officer of a corporation, in the absence of express provision or agreement, is not entitled to compensation for performing the ordinary duties of his office; but he can recover, on an implied contract, the value of extraordinary services rendered at the request of the corporation. Express provision is usually made for the compensation of officers. An officer of a corporation cannot fix his own salary.

⁸⁶⁸ *Morgan v. Skiddy*, 62 N. Y. 319. The publication by savings bank directors that the directors and stockholders are personally responsible for its debts does not constitute a contract with depositors, but, if intentionally false, affords the basis of an action of deceit. *Westervelt v. Demarest*, 46 N. J. Law, 37.

⁸⁶⁹ *Wakeman v. Dalley*, 51 N. Y. 27; *Arthur v. Griswold*, 55 N. Y. 400; *Cowley v. Smyth*, 46 N. J. Law, 380; *Cole v. Cassidy*, 138 Mass. 437; *Zinn v. Mendel*, 9 W. Va. 580.

⁸⁷⁰ *Wakeman v. Dalley*, 51 N. Y. 27.

⁸⁷¹ *Clark*, Cont. 324.

⁸⁷² *People v. England*, 27 Hun (N. Y.) 139.

When a director or other officer of a corporation performs the usual and ordinary duties of his office, as defined by the charter or by-laws, he cannot recover any compensation therefor, unless it has been so specially agreed. He cannot, in such a case, recover, on an implied contract, what the services were reasonably worth.³⁷³ But if an officer, at the request of the corporation, performs extraordinary services, not within the usual duties of his office, he may recover therefor without a special agreement. Thus, a director of a railroad company, who, at its request, rendered services as an attorney, and in procuring aid notes, right of way, etc., was held to be entitled to recover the reasonable value of such services, on an implied contract, as they were not embraced in his ordinary duties as director.³⁷⁴

Unless otherwise provided in the charter or by-laws of the corporation, the power to fix the salaries of the officers of the corporation vests in the board of directors. In doing so they must act in good faith, and for the benefit of the corporation. They have no authority to pay claims which the corporation is under no obligation to pay. Thus, they cannot pay an officer anything for past services, which have been rendered and paid for at a fixed salary previously agreed.³⁷⁵ In some jurisdictions, as we have seen, if they fix their own salaries as officers, where they occupy other positions, such as that of president, secretary, etc., the transaction may be repudiated, at the election of the corporation, and this without regard to whether they acted in good faith or not.³⁷⁶ In other jurisdictions, perhaps, in the absence of any provision in the charter or by-laws, they may fix their salaries as officers of the company, and the transaction will be sustained, if in perfect good faith and free from any suspicion of fraud or unfairness; but, if there is any bad faith or unfairness, their act will be set aside, at the election of the corporation.³⁷⁷ An officer who is also a director

³⁷³ *Citizens' Nat. Bank v. Elliott*, 55 Iowa, 104, 7 N. W. 470; *American Cent. Ry. Co. v. Miles*, 52 Ill. 174; *Cheaney v. Railway Co.*, 68 Ill. 570; *Holder v. Railway Co.*, 71 Ill. 106; *New York & N. H. R. Co. v. Ketchum*, 27 Conn. 170.

³⁷⁴ *Ten Eyck v. Railroad Co.*, 74 Mich. 226, 41 N. W. 905. And see *Cheaney v. Railway Co.*, 68 Ill. 570; *Lafayette, B. & M. Ry. Co. v. Cheaney*, 87 Ill. 446.

³⁷⁵ *Jones v. Morrison*, 31 Minn. 140, 16 N. W. 854.

³⁷⁶ *Ante*, p. 508.

³⁷⁷ *Jones v. Morrison*, 31 Minn. 140, 16 N. W. 854.

is not qualified to vote at a meeting of the board on a resolution fixing his salary.³⁷⁸

REMOVAL OF OFFICERS AND AGENTS.

212. The principal rules in regard to the removal of officers and agents of a corporation are these:

- (a) A corporation has a right to remove an officer or agent, where there is a contract for a fixed term, only where he violates his contract, or is incompetent. But it can at any time revoke the authority of an agent, rendering itself liable for breach of contract.
- (b) An officer or agent who is appointed by vote of the stockholders, or whose tenure is fixed by the charter, cannot be removed, nor his authority revoked, by the directors.
- (c) In some states, by express provision, the directors may remove their own appointees at pleasure, and they may do so without such a provision in the absence of a contract for a fixed time.
- (d) In some jurisdictions a court of equity will remove a director whose election is void, but, by the better opinion, the remedy is at law, by quo warranto, and a court of equity will grant relief only where it has acquired jurisdiction on some other ground.

Officers and agents of a corporation who do not hold their office under contract for a fixed time may be removed at pleasure by the corporation, or by the superior officer or officers who appointed them.³⁷⁹ But, if there is a contract for a fixed term between an officer and the corporation, he cannot be removed without cause,

³⁷⁸ Jones v. Morrison, 81 Minn. 140, 16 N. W. 854; Miner v. Ice Co., 93 Mich. 97, 58 N. W. 218; ante, p. 493.

³⁷⁹ 1 Thomp. Corp. §§ 802, 805.

without rendering the corporation liable for breach of contract. In such a case, like any other employé, he may be removed for cause, as for breach of contract or incompetency. And it seems that a corporation, like any other principal, may at any time revoke the authority of its officer or agent, subject to liability for breach of contract.⁸⁸⁰ If the tenure of a person to a corporate office is fixed by charter, and there is no provision for removal, there is no power to remove him until his term of office expires. If an officer is appointed by vote of the stockholders the directors have no implied authority to remove him.⁸⁸¹

By the weight of authority, a court of equity will not primarily take jurisdiction to determine the legality of an election of directors, or to remove a director who is in possession of the office.⁸⁸² The court will inquire into the regularity of the election, or the right of the person to the office, only when the question arises incidentally and collaterally in a suit of which the court has rightful jurisdiction, and the grant of the relief depends upon its decision. If the right to the office only is in question, the remedy is at law, by quo warranto.⁸⁸³

RELATION BETWEEN OFFICERS AND STOCKHOLDERS.

213. The officers of a corporation are not the agents of the stockholders, but of the corporation; nor do they occupy a fiduciary relation towards the stockholders individually.

It is often said that the directors of a corporation are trustees of the stockholders, and that the relation of trustee and cestui que trust,

⁸⁸⁰ Id. § 805.

⁸⁸¹ Id. § 804.

⁸⁸² As to the grounds of removal, and the mode of exercising the power, see 1 *Thomp. Corp.* §§ 806-841.

⁸⁸³ *Perry v. Oil-Mill Co.*, 98 Ala. 364, 9 South. 217; *Nathan v. Tompkins*, 82 Ala. 437, 2 South. 747; *Johnston v. Jones*, 23 N. J. Eq. 216; *Neall v. Hill*, 16 Cal. 145, 76 Am. Dec. 508. But see *Wright v. Water Co.*, 67 Cal. 532, 8 Pac. 70, where it was held that a court of equity has jurisdiction of a bill to set aside an illegal election, though no other ground of jurisdiction exist.

with its consequences, exists between them, but they do not occupy any such relation towards the stockholders individually. They are simply the agents of the corporation. There is no privity, in law, between them and the stockholders. They are not the agents of the stockholders, but of the corporation,—of the legal entity. And, when it is said that they are trustees for the stockholders, it can only be meant that they occupy a fiduciary relation to the corporation, and that they are bound to act for the benefit of all the shareholders alike, and not for their own advantage, nor for the advantage of particular shareholders to the exclusion of others. “There is,” said Chief Justice Shaw, “no legal privity, relation, or immediate connection between the holders of shares in a bank, in their individual capacity, on the one side, and the directors of the bank, on the other. The directors are not the bailees, the factors, agents, or trustees of such individual stockholders.”⁸⁸⁴ If they commit a breach of trust, the injury, in the eye of the law, is to the corporation, and primarily the corporation is the proper party to sue for redress. It is well settled that an action at law cannot be maintained by a stockholder against a director or other officer of the corporation for fraud, negligence, misapplication of funds, or other wrongs resulting in injury to the corporation. Such an action can only be maintained by the corporation, the injury being to it; and it can make no difference in such a case, that the value of the shares is diminished, and that the stockholder therefore individually suffers a loss.⁸⁸⁵ The directors of a bank, said the Connecticut court, in such a case, “are the agents of the bank. The bank is the only principal, and there is no such trust for or relation to a stockholder as has been claimed by the plaintiff. The entire duty of the directors, growing out of their agency, is owed to the bank, which, under the charter, is the sole representative of the stockholders, and the legal protector and defender of their property.”⁸⁸⁶ As we have seen, if the agents of the corporation will not or cannot sue for injuries to it, so that such injuries cannot be redressed

⁸⁸⁴ *Smith v. Hurd*, 12 Metc. (Mass.) 371, 1 Cumming, Cas. Priv. Corp. 792.

⁸⁸⁵ *Smith v. Hurd*, 12 Metc. (Mass.) 371, 1 Cumming, Cas. Priv. Corp. 792; *Allen v. Curtis*, 26 Conn. 456.

⁸⁸⁶ *Allen v. Curtis*, *supra*.

through the corporate body, a court of equity will look behind the corporation, and recognize the stockholders, and will allow them to sue in their own names.³⁸⁷

An officer of a corporation occupies no fiduciary relation towards an individual stockholder, so as to impose upon him, in dealing with the stockholder as an individual, any duties which he would not owe to strangers. Thus, where the president of a corporation, who was also a director, having knowledge through his official position that the company's stock was worth more than its nominal market value, purchased stock from a stockholder for the market price, without disclosing to him the facts within his knowledge as to the real value, it was held that there was, in such transaction, no fiduciary relation between him and the stockholder, binding him to make such a disclosure, and that, in the absence of actual fraud, the purchase was valid.³⁸⁸

³⁸⁷ Ante, p. 389.

³⁸⁸ Board of Commissioners of Tippecanoe County v. Reynolds. 44 Ind. 509.

CHAPTER XIV.

RIGHTS AND REMEDIES OF CREDITORS.

- 214. Relation between Creditors and the Corporation—Remedies in General.
- 215. Property Subject to Execution.
- 216. Assets of a Corporation as a "Trust Fund" for Creditors.
- 217. Interference in Management of Corporation.
- 218. Fraudulent Conveyances and Transfers.
- 219. Suits for Injunction and Receiver.
- 220. Assignment for Benefit of Creditors—Preferences.
- 221. Dissolution of Corporation.
- 222. Consolidation of Corporations.
- 223. Extension of Charter—New Corporation.
- 224. Set-Off by Debtor of Corporation.
- 225–226. Relation between Creditors and Stockholders.
- 227–230. Statutory Liability of Stockholders.
 - 231. Who are Liable as Stockholders under the Statutes.
- 232–233. Who may Enforce Statutory Liability.
- 234–236. Remedies of Creditors against Stockholders.
 - 237. Necessity for Judgment against Corporation.
 - 238. Effect of Judgment against Corporation.
 - 239. Statute of Limitations.
 - 240. Set-Off by Stockholders.
 - 241. Contribution among Stockholders.
- 242–243. Relation between Creditors and Officers.
 - 244. Preferences to Officers Who are Creditors.
 - 245. Statutory Liability of Officers.

RELATION BETWEEN CREDITORS AND THE CORPORATION —REMEDIES IN GENERAL.

214. Generally the creditors of a corporation have the same rights and remedies against the corporation and its property as if it were a natural person.
Thus,

(a) They may obtain judgment against it, and enforce the same

(1) At law, by execution against its property.

(2) In equity, by bill to subject equitable assets of the corporation, which cannot be reached by execution.

(b) They may proceed by attachment where by statute they may so proceed against a natural person.

As a general rule the rights and remedies of the creditors of a corporation against it are the same, both at law and in equity, as the rights and remedies of the creditors of a natural person are against him. They may sue the corporation at common law, and recover a judgment against it, and may enforce the judgment by execution against the corporate assets.¹ Like creditors of a natural person, also, they may come into a court of equity and reach and subject equitable assets of the corporation to the satisfaction of their claims.² Creditors of a corporation may also attach the property of a corporation under the statutes, where the property of a natural person could be attached. A corporation is a "person," within the meaning of the attachment laws.³

SAME—PROPERTY SUBJECT TO EXECUTION.

215. The property of a corporation is subject to seizure and sale on execution against it, with this exception:

EXCEPTION—At common law neither the franchises of a corporation, nor property that is necessary to enable it to exercise its franchises, are subject to execution. This has been very generally changed by statute.

Ordinarily the property of a corporation may be seized on execution by its creditors to the same extent, and in the same manner, as the property of a natural person.⁴ But there are some exceptions. At common law the franchises of a corporation are not subject to seizure

¹ As to what property is subject to execution, see section 215, *infra*.

² Post, pp. 549, 559, 563.

³ Mineral Point R. Co. v. Keep, 22 Ill. 9; ante, p. 24.

⁴ Plymouth R. Co. v. Colwell, 89 Pa. St. 337.

and sale upon execution. Nor can lands, easements, or things essential to the existence of the corporation and the execution of its corporate duty, and without which its franchise would be of no practical use, be levied upon and sold on execution at law, so as to detach them from the franchise, and thus destroy its use.⁵ Accordingly, where, upon an execution issued on a judgment recovered against a canal company, the marshal seized and advertised for sale a toll house and sundry canal locks, and other tangible property, an injunction was granted to prevent the sale; the court holding that, in the absence of a statute, neither the franchise of the company, nor any lands or works essential to the enjoyment of the franchise, and which could not be separated from it without destroying or impairing its value, could be sold on execution.⁶ So it has been held as to the right of way of a railroad company.⁷ In most jurisdictions this rule of the common law is changed by express statutory provisions.

**SAME—ASSETS OF A CORPORATION AS A “TRUST FUND”
FOR CREDITORS.**

216. The capital stock and assets of a corporation belong to it, and may be disposed of by it, if it does not violate its charter, as fully and as freely as if it were a natural person, subject only to the right of creditors to attack transactions as fraudulent. No direct trust attaches to its property in favor of its creditors.

In most of the text-books, and in a great number of the cases, it is said broadly, and without qualification, that the capital stock and assets of a corporation constitute a “trust fund” for the payment of its creditors, and cannot be squandered or given away when necessary for the satisfaction of their claims.⁸ And it is also said (applying

⁵ *Louisville, N. A. & C. Ry. Co. v. Boney*, 117 Ind. 501, 20 N. E. 432; *Gue v. Canal Co.*, 24 How. 257; *East Alabama Ry. Co. v. Doe*, 114 U. S. 340, 5 Sup. Ct. 869; *Overton Bridge Co. v. Means*, 33 Neb. 857, 51 N. W. 240.

⁶ *Gue v. Canal Co.*, *supra*.

⁷ *East Alabama Ry. Co. v. Doe*, *supra*.

⁸ *Wood v. Dummer*, 3 Mason, 308, Fed. Cas. No. 17,944, 1 Cumming, Cas. Priv. Corp. 805; *Sanger v. Upton*, 91 U. S. 56; *Camden v. Stuart*, 144 U. S. 104,

the equitable rule by which trust funds may be followed)⁹ that, if this is done, the property may be followed in equity by the creditors of the corporation into the hands of any person other than a bona fide purchaser for value.¹⁰ Late decisions, however, and a careful consideration of most of the cases in which this dictum may be found, will show that in reality both the capital stock of a corporation and its other assets—so long, at least, as it is doing business—belong to the corporation itself, both in law and in equity, just as completely as does the property of a natural person belong to him, and they are not, in any true sense, held in trust for its creditors.

The doctrine that the capital stock of a corporation is a trust fund for creditors was first laid down by Mr. Justice Story in *Wood v. Dummer*.¹¹ In this case a bank had distributed part of its capital stock among its stockholders, leaving debts unpaid, and nothing with which to pay them. It was said that the property so distributed was a trust fund for the payment of the debts of the corporation, and it was held that the creditors could follow it in equity into the hands of the stockholders. The doctrine was thus stated: "It appears to me very clear upon general principles, as well as the legislative intention, that the capital stock of banks is to be deemed a pledge or trust fund for the payment of the debts contracted by the bank. The public, as well as the legislature, have always supposed this to be a fund appropriated for such purpose. The individual stockholders are not liable for the debts of the bank, in their private capacities. The charter relieves them from personal responsibility, and substi-

12 Sup. Ct. 585; *Hightower v. Thornton*, 8 Ga. 486; *Briggs v. Penniman*, 8 Cow. (N. Y.) 387; *Slee v. Bloom*, 19 Johns. (N. Y.) 456; *Bartlett v. Drew*, 57 N. Y. 587; *Hastings v. Drew*, 76 N. Y. 9; *Cole v. Iron Co.*, 133 N. Y. 164, 30 N. E. 847; *Nevitt v. Bank*, 6 Smedes & M. (Miss.) 513; *Marshall Foundry Co. v. Killian*, 99 N. C. 501, 6 S. E. 680; *Ohio Life Ins. & Trust Co. v. Merchants' Ins. & Trust Co.*, 11 Humph. (Tenn.) 1; *State v. Commercial State Bank*, 28 Neb. 677, 44 N. W. 998.

⁹ Fetter, Eq. 207-209.

¹⁰ *Wood v. Dummer*, 3 Mason, 308, Fed. Cas. No. 17,944, 1 Cumming, Cas. Priv. Corp. 805; *Cole v. Iron Co.*, 133 N. Y. 164, 30 N. E. 847; *Hibernia Ins. Co. v. St. Louis & New Orleans Transp. Co.*, 13 Fed. 516; *Montgomery Web Co. v. Dienelt*, 133 Pa. St. 585, 19 Atl. 428; *Vance v. Coke Co.*, 92 Tenn. 47, 20 S. W. 424; *Fisk v. Railroad Co.*, 10 Blatchf. 518, Fed. Cas. No. 4,830.

¹¹ 3 Mason, 308, Fed. Cas. No. 17,944, 1 Cumming, Cas. Priv. Corp. 805.

tutes the capital stock in its stead. Credit is universally given to this fund by the public as the only means of repayment. During the existence of the corporation it is the sole property of the corporation, and can be applied only according to its charter; that is, as a fund for payment of its debts, upon the security of which it may discount and circulate notes. Why, otherwise, is any capital stock required by our charters? If the stock may, the next day after it is paid in, be withdrawn by the stockholders, without payment of the debts of the corporation, why is its amount so studiously provided for, and its payment by the stockholder so diligently required? To me this point appears so plain, upon principles of law as well as common sense, that I cannot be brought into any doubt that the charters of our banks make the capital stock a trust fund for the payment of all the debts of the corporation. The billholders and other creditors have the first claims upon it, and the stockholders have no rights until all the other creditors are satisfied. They have the full benefit of all the profits made by the establishment, and cannot take any portion of the fund until all the other claims on it are extinguished. Their rights are not to the capital stock, but to the residuum after all demands on it are paid. On a dissolution of the corporation the billholders and the stockholders have each equitable claims, but those of the billholders possess, as I conceive, a prior, exclusive equity."

This is the decision and the dictum upon which the so-called trust-fund doctrine is based. But it requires no argument to show that the facts of the case did not render it necessary to hold the capital stock of a corporation a trust fund for creditors, in the strict sense of the term. All that the case decided was that a corporation cannot distribute its capital stock among its stockholders, and thereby leave creditors unpaid,—a transaction which is clearly a fraud upon existing creditors, just as a voluntary conveyance by a natural person is a fraud upon his existing creditors, who are thereby prevented from collecting their claims. So, if a corporation releases subscribers from liability to contribute to the capital stock, or distributes part of the capital stock to them, the transaction is a fraud upon subsequent creditors who are ignorant of the transaction, and deal with it on the faith of its capital stock being fully paid, and the transaction may be avoided by them on this ground. Many of the courts base the right of creditors to hold stockholders liable in these cases upon the

ground that the capital stock is a trust fund for creditors. And it is in these cases, chiefly, that we find the trust-fund doctrine declared.¹² No such doctrine, however, is necessary. The stockholders are liable on the ground of fraud. Persons who deal with a corporation and become its creditors after such a transaction, and with knowledge of it, cannot complain, because they are not defrauded.¹³ If the capital stock were really a trust fund for creditors, they could complain.

Other cases in which the doctrine is announced, and seemingly relied upon, are cases in which the corporation has transferred its property to third persons in fraud of creditors.¹⁴ Thus, in *Cole v. Millerton Iron Co.*,¹⁵ a corporation had transferred all its property to another corporation, having the same officers and stockholders, pending an action against it, which afterwards resulted in a judgment. The only consideration for the transfer was the assumption by the grantee of the grantor's debts. The court, in holding the transfer illegal and void as against this judgment creditor, said, "The assets of a corporation are a trust fund for the payment of its debts, upon which the creditors have an equitable lien, both as against the stockholders and all transferees except those purchasing in good faith and for value." Clearly, it was unnecessary to resort to any trust-fund theory to sustain this decision.

The trust-fund doctrine has been virtually repudiated by the supreme court of Minnesota in the late case of *Hospes v. Northwestern Manuf'g & Car Co.*; ¹⁶ Judge Mitchell, one of the ablest jurists on the bench, delivering the opinion of the court. It was held that the capital stock of a corporation is its own property, which it may use and dispose of, if not prohibited by its charter, the same as a natural person; that it is not held in trust for creditors, except in the sense that there can be no distribution of it among stockholders without pro-

¹² Such is the case in *Wood v. Dummer*, 3 Mason, 308, Fed. Cas. No. 17,944, 1 Cumming, Cas. Priv. Corp. 805; *Sanger v. Upton*, 91 U. S. 56; *Camden v. Stuart*, 144 U. S. 104, 12 Sup. Ct. 585; *Slee v. Bloom*, 19 Johns. (N. Y.) 456; *Bartlett v. Drew*, 57 N. Y. 587; *Hastings v. Drew*, 76 N. Y. 9; and in most of the other cases in which the doctrine is announced.

¹³ *Hospes v. Car Co.*, 48 Minn. 174, 50 N. W. 1117.

¹⁴ *Sutton Manuf'g Co. v. Hutchinson*, 11 C. C. A. 320, 63 Fed. 496, Shep. Cas. Corp. 229.

¹⁵ 133 N. Y. 164, 30 N. E. 847.

¹⁶ 48 Minn. 174, 50 N. W. 1117.

vision being first made for the payment of corporate debts; and that, as in the case of a natural person, any disposition of it in fraud of creditors is void. "The phrase," said Judge Mitchell, "that 'the capital of a corporation constitutes a trust fund for the benefit of creditors,' is misleading. Corporate property is not held in trust, in any proper sense of the term. A trust implies two estates or interests,—one equitable and one legal; one person, as trustee, holding the legal title, while another, as the cestui que trust, has the beneficial interest. Absolute control and power of disposition are inconsistent with the idea of a trust. The capital of a corporation is its property. It has the whole beneficial interest in it, as well as the legal title. It may use the income and profits of it, and sell and dispose of it, the same as a natural person. It is a trustee for its creditors in the same sense and to the same extent as a natural person, but no further."

In *Sanger v. Upton*,¹⁷ in the supreme court of the United States, it was said, in substance, as by Mr. Justice Story in *Wood v. Dummer*:¹⁸ "The capital stock of an incorporated company is a fund set apart for the payment of its debts. It is a substitute for the personal liability which subsists in private co-partnerships. When debts are incurred, a contract arises with the creditors that it shall not be withdrawn, or applied otherwise than upon their demands, until such demands are satisfied. The creditors have a lien upon it in equity. If diverted, they may follow it as far as it can be traced, and subject it to the payment of their claims, except as against holders who have taken it bona fide for a valuable consideration, and without notice. It is publicly pledged to those who deal with the corporation for their security. Unpaid stock is as much a part of this pledge, and as much a part of the assets of the company, as the cash which has been paid in upon it. Creditors have the same right to look to it as to anything else, and the same right to insist upon its payment as upon the payment of any other debt due to the company. As regards creditors, there is no distinction between such a demand and any other assets which may form a part of the property and effects of the corporation." This dictum is broad enough to imply that all the assets of a corporation constitute a trust fund, in the strict sense, for the payment of its debts, but it must be taken in connection with the facts before the

¹⁷ 91 U. S. 56.

¹⁸ 3 Mason, 308, Fed. Cas. No. 17,944, 1 Cumming, Cas. Priv. Corp. 805.

court. Except as applied to them, it is mere dictum. In this case the assignee in bankruptcy of a corporation was seeking to compel stockholders to pay a balance due for their stock. It was merely an effort to reach debts due to the corporation,—equitable assets of the corporation,—and apply them in payment of its debts. There was no necessity at all to resort to any trust-fund doctrine. And the later decisions of the supreme court of the United States clearly show that they do not regard corporate assets as a trust fund for the payment of debts. Thus, it has been held that persons who become creditors of a corporation, with knowledge that its stock has not been paid in full, and that it was issued under an agreement by which the stockholders are not bound, as between them and the corporation, to pay it in full, cannot compel further payments.¹⁹ The reason is that no fraud is committed upon them. If the capital stock were a trust fund for their benefit, they could compel payment in such a case. So it has been held that a conveyance of its property by a corporation cannot be questioned by those who subsequently deal with it.²⁰ Such rulings as these are inconsistent with the so-called trust-fund doctrine.

It may, perhaps, be said that the capital stock of a corporation is a trust fund for creditors who deal with it on the faith of its being full paid, and that it is on this ground that they may compel its payment notwithstanding any contrary agreement by the corporation. It is not necessary, however, to rest their right in this respect on any trust-fund theory, and to do so merely tends to confuse. Their right in such a case may well be rested on the ground of fraud. As was said by Judge Mitchell: "By putting it upon the ground of fraud, and applying the old and familiar rules of law on that subject to the peculiar nature of a corporation, and the relation which its stockholders bear to it and to the public, we have at once rational and logical ground on which to stand. The capital of a corporation is the basis of its credit. It is a substitute for the individual liability of those who own its stock. People deal with it and give it credit on the faith of it. They have a right to assume that it has paid-in capital to the amount which it represents itself as having, and if they give it credit on the faith of that representation, and if the representation

¹⁹ *Hospes v. Car Co.*, 48 Minn. 174, 50 N. W. 1117.

²⁰ *Post*, p. 550.

rule that simple-contract creditors cannot come into equity to obtain the seizure of their debtor's property, and its application to their claims, applies with the same force when the debtor is a corporation; and the rule is not changed by the insolvency of the corporation, its failure to collect in full all stock subscriptions, its execution of an illegal trust deed, or the pendency in the same court of a suit to foreclose the same, for neither of these things, nor all together, operates to charge upon the corporation's property any lien or direct trust in favor of simple-contract creditors.

SAME—INTERFERENCE IN MANAGEMENT OF CORPORATION.

217. The creditors of a corporation have no right, either at law or in equity, merely because they are creditors, to interfere in its management, or to come into a court of equity to restrain it from making contracts or disposing of its property, unless there is fraud or breach of trust to give a court of equity jurisdiction.

This rule seems to be well settled.²⁸ The property of a corporation, so long at least as it is doing business, belongs to it as fully as the property of a natural person belongs to him, and, as a rule, it may make contracts and dispose of its property to the same extent as a natural person. If it makes conveyances or transfers of property on which creditors have a lien, or if it makes them, not in good faith, but with intent to hinder and delay its creditors, they may come into a court of equity, after obtaining judgment, and obtain relief by subjecting the property to the satisfaction of the judgment, just as the creditors of a natural person may do. Or, if the remedy is given by statute, they may proceed by attachment, and in that way secure their claim. But, in the absence of fraud or breach of trust, the creditors of a corpora-

²⁸ See *Mills v. Buenos Ayres Co.*, 5 Ch. App. 621, 1 Cumming, Cas. Priv. Corp. 993; *Pond v. Railroad Co.*, 130 Mass. 194, 1 Cumming, Cas. Priv. Corp. 1005; *Hollins v. Iron Co.*, 150 U. S. 371, 14 Sup. Ct. 127; *Hospes v. Car Co.*, 48 Minn. 174, 50 N. W. 1117; *Tawas & B. C. R. Co. v. Iosco Circuit Judge*, 44 Mich. 479, 7 N. W. 65.

be called on to interfere with the concerns of almost every company in the kingdom against which a creditor might suppose that he had demands which he had not established in a court of justice, but which he was about to proceed to establish. If there is this power in any case, of course, it would apply, not only to the raising of money by debentures and to paying shareholders, but it would extend to an interference in every possible way with the dealings of the company."

A similar decision was made by the Massachusetts court in *Pond v. Framingham & Lowell Railroad Co.*²⁵ In that case a creditor of a corporation sought to enjoin it from making leases, on the ground that they would remove property from his reach in enforcing his claim. The court said: "The plaintiffs cannot maintain this bill, unless upon the ground that any creditor can maintain a bill in equity against an individual debtor upon like allegations. But there is no allegation of fraud or breach of trust, or any other ground of jurisdiction which brings the case within the general equity powers of a court of chancery. The bill is an attempt by a creditor to restrain his debtor from making what is alleged to be an improvident contract. The rights of the parties are governed by the rules of the common law. The plaintiffs, as creditors, might, by an attachment, have obtained security which would take precedence of the contemplated lease; but, if they could not, the court has no power to restrain the debtor from making a disposition of his property which is permitted by the common law, unless fraud or a breach of trust is alleged and shown. The allegation that the defendant corporation is insolvent does not aid the plaintiffs. In the absence of any statute giving the power, this court has no authority to act as a court of insolvency for the liquidation of the affairs of an insolvent railroad corporation."

²⁵ 130 Mass. 194, 1 Cumming, Cas. Priv. Corp. 1005.

SAME—FRAUDULENT CONVEYANCES AND TRANSFERS.

218. Conveyances and transfers of its property by a corporation with intent to hinder, delay, and defraud its creditors are invalid to the same extent, and on the same principles, as fraudulent conveyances and transfers by a natural person. As a rule,

- (a) They can be questioned, and the property reached, only by persons who were creditors at the time they were made.
- (b) Before a creditor can come into equity to set them aside and subject the property to his claim, he must have recovered a judgment against the corporation, and issued execution thereon.

If a corporation conveys or transfers its property fraudulently, with intent to hinder or delay creditors in the enforcement of their claims, they may come into a court of equity and set aside the transaction, as against any person other than a bona fide purchaser for value, and subject the property so disposed of to the satisfaction of their claims. They have such rights, and such rights only, in this respect, as the creditors of a natural person would have under the same circumstances. The principles of law which govern are the same in both cases.²⁶

The stockholders of a corporation cannot transfer the corporate property to themselves, directly or indirectly, and so defeat the rights of creditors of the corporation. And they cannot do this by forming a new corporation in which they are the principal stockholders, and procuring a transfer to it of the property of the old company. Such a transfer is a fraud upon the creditors of the old company, and may be treated as void as to them, or the new corporation may be held liable for the debts of the old, to the extent of the property received by it.²⁷ But where a new corporation is formed, and purchases the assets of the old company, the new company cannot be made to satisfy

²⁶ *Graham v. Railroad Co.*, 102 U. S. 148, 1 Cumming, Cas. Priv. Corp. 1006; *Sutton Manuf'g Co. v. Hutchinson*, 11 C. C. A. 320, 63 Fed. 496, Shep. Cas. Corp. 229.

²⁷ *Montgomery Web Co. v. Dienelt*, 133 Pa. St. 585, 19 Atl. 428; *Hibernia*

a judgment recovered against the old company for a cause of action arising after the transfer.²⁸

Subsequent Creditors.

A conveyance made with intent to defraud persons to whom the grantor expects to become immediately or soon indebted may be attacked and avoided by such person in a proper case. But it is a well-settled rule of law that if an individual, being solvent at the time, without any actual intent to defraud creditors, dispose of property for an inadequate consideration, or even make a voluntary conveyance of it, subsequent creditors cannot question the transaction, for they are not injured thereby. They are presumed to give credit to the debtor in the status which he has after the conveyance. In *Graham v. La Crosse & M. R. Co.*,²⁹ it was held that this principle applies to conveyances by a corporation; that the disposal by a corporation of any of its property cannot be questioned by subsequent creditors any more than a like disposition of property by an individual may be. It was contended in this case that a corporation debtor does not stand on the same footing as an individual debtor; that, while the latter has supreme dominion over his own property, a corporation is a mere trustee, holding its property for the benefit of the stockholders and creditors; and that if it fail to pursue its rights against third persons, whether arising out of fraud or otherwise, it is a breach of trust, and creditors may come into equity to compel an enforcement of the corporate duty. "We do not concur in this view," it was said. "It is at war with the notions which we derive from the English law with regard to the nature of corporate bodies. A corporation is a distinct entity. Its affairs are necessarily managed by officers and agents, it is true; but, in law, it is as distinct a being as an individual

Ins. Co. v. St. Louis & N. O. Transp. Co., 13 Fed. 516; *Vance v. Coke Co.*, 92 Tenn. 47, 20 S. W. 424; *Brum v. Insurance Co.*, 16 Fed. 140. And see, to the same effect, where the members of an embarrassed firm formed a corporation, and transferred to it the partnership property. *Booth v. Bunce*, 33 N. Y. 139. And see *Reed Bros. Co. v. First Nat. Bank*, 46 Neb. 168, 64 N. W. 701. Cf. *Campbell v. Bank (Neb.)* 68 N. W. 344.

²⁸ *Gray v. Steamship Co.*, 115 U. S. 116, 5 Sup. Ct. 1166. But where a corporation, while a going concern, but without property enough to pay its debts, and when all believed that its continuance would bring financial success, executes a mortgage to its directors, sureties on its notes, to secure them and induce renewals and further advances, the mortgage is not invalid. *Sanford Fork & Tool Co. v. Howe, Brown & Co.*, 157 U. S. 312, 15 Sup. Ct. 621.

²⁹ 102 U. S. 148, 1 Cumming, Cas. Priv. Corp. 1006.

gether, operate to charge any lien or direct trust in favor of simple-contract creditors.³²

SAME—SUITS FOR INJUNCTION AND RECEIVER.

219. Creditors who have recovered judgment against a corporation, and exhausted their legal remedy, and, in very exceptional cases, simple-contract creditors, may maintain a bill in equity to reach assets of an insolvent corporation which have been unlawfully diverted, and, if necessary, a receiver may be appointed. A court of equity may also restrain a threatened diversion of property in such a case.

We have just seen that, where the officers of an insolvent corporation have fraudulently and illegally diverted its property, creditors who have obtained judgments against the corporation, on which execution has been returned unsatisfied, may maintain a bill in equity to reach such property and subject it to the payment of their claims, as against any person who is not a bona fide purchaser for value. In such a suit, if necessary, the court may appoint a receiver to take charge of the corporate assets, collect debts due the corporation, and make distribution.³³ Jurisdiction in such a case is very generally conferred by statute.

There are a number of cases in which it has been held, upon the theory that the assets of a corporation are a trust fund for the payment of its debts, that where the officers of a corporation are about to commit waste, or divert the assets of the corporation, when it is insolvent, and thereby cause irreparable loss to creditors, the creditors may come into a court of equity and obtain an injunction to restrain the threatened diversion and the appointment of a receiver, if this is necessary to control and secure the corporate property to the payment of its debts.³⁴ And it has been held that such a suit may

³² *Hollins v. Iron Co.*, *supra*.

³³ *Turnbull v. Lumber Co.*, 55 Mich. 387, 21 N. W. 375.

³⁴ 2 Mor. Priv. Corp. §§ 797-799; *Conro v. Gray*, 4 How. Prac. (N. Y.) 168; *Covington Drawbridge Co. v. Shepherd*, 21 How. 112; *Gaylord v. Railroad Co.*, Fed. Cas. No. 5,284; *Fisk v. Railroad Co.*, Id. 4,830; *Irons v. Bank*, Id. 7,068.

tion which has become insolvent and ceased to do business cannot prefer certain creditors over others, either by mortgage, provision in an assignment for the benefit of creditors, or otherwise.⁴⁰ By the weight of authority, however, the rights and powers of a corporation in this respect are identical with those of an individual, and it may lawfully prefer particular creditors, unless prohibited by statute.⁴¹ In a number of states the question has been settled by express statutory prohibition against preferences.⁴² The effect of preferences to officers who are creditors is elsewhere considered.⁴³

⁴⁰ *Rouse v. Bank*, 46 Ohio St. 493, 22 N. E. 293; *Lyons-Thomas Hardware Co. v. Perry Stove Manuf'g Co.*, 86 Tex. 143, 24 S. W. 16, Shep. Cas. Corp. 235; *Thompson v. Lumber Co.*, 4 Wash. St. 600, 30 Pac. 741.

⁴¹ *Bank of Montreal v. J. E. Potts Salt & Lumber Co.*, 90 Mich. 345, 51 N. W. 512 (collecting cases); *Catlin v. Bank*, 6 Conn. 233; *Wilkinson v. Bauerle*, 41 N. J. Eq. 635, 7 Atl. 515; citing *Sargent v. Webster*, 13 Metc. (Mass.) 497; *Dana v. Bank*, 5 Watts & S. (Pa.) 223; *Arthur v. Bank*, 9 Smedes & M. (Miss.) 394; *Town v. Bank of River Raisin*, 2 Doug. (Mich.) 530; *Buell v. Buckingham*, 16 Iowa, 284. And see *Vail v. Jameson*, 41 N. J. Eq. 648, 7 Atl. 520; *Warfield v. Canning Co.*, 72 Iowa, 666, 34 N. W. 467; *Rollins v. Carriage Co.*, 80 Iowa, 380, 45 N. W. 1037; *State v. Bank*, 6 Gill & J. (Md.) 205; *Coats v. Donnell*, 94 N. Y. 168, 178; *Sells v. Commission Co.*, 72 Miss. 590, 17 South. 236; *Foster v. Planing-Mill Co.*, 92 Mo. 79, 4 S. W. 260; *Reichwald v. Hotel Co.*, 106 Ill. 439; *Glover v. Lee*, 140 Ill. 102, 29 N. E. 680. And cf. *Hollins v. Iron Co.*, 150 U. S. 371, 14 Sup. Ct. 127.

⁴² *Throop v. Lithographic Co.*, 125 N. Y. 530, 26 N. E. 742; *Scott v. Armstrong*, 146 U. S. 499, 13 Sup. Ct. 148, Shep. Cas. Corp. 50. In New York it is provided that, whenever a corporation shall have refused payment of a debt, it shall not be lawful for it, or any of its officers, to assign or transfer any of its property or choses in action to any of its officers or stockholders, directly or indirectly, for the payment of any debt; and it shall not be lawful to make any transfer or assignment in contemplation of insolvency to any person or persons whatever. In *Varnum v. Hart*, 119 N. Y. 101, 23 N. E. 183, the New York court, construing this provision, held that it put no restraint upon creditors, but only upon the affirmative action of the corporation and its officers; and it appearing in this case that creditors of a corporation, knowing it to be insolvent, arranged with an officer thereof that he should not disclose service of summons on him, and afterwards obtained judgment by default, and sold property of the corporation on execution, it was held not to be a violation of the statute. This provision, it has been held, renders void an attachment against an insolvent corporation by a creditor, who is one of its directors, though he has no control over its assets, and though the proceed-

⁴³ Post, p. 608.

SAME—DISSOLUTION OF CORP.

221. At common law, dissolution of a corporation extinguishes its debts; but it is otherwise very generally by statute. In a dissolved corporation may be made payment of its debts.

At common law, debts due to and from a corporation are extinguished by its dissolution. This must necessarily be so, for in solution there is no one, in law, to sue or be sued, and, ever, does not obtain in equity. A court of equity will not enforce debts due to the corporation, and will not apply its assets to the payment of its debts.⁴⁴

The dissolution of a corporation, as we have seen, is by charter or statutory authority, cannot be objected to on the ground of impairment of the obligation of their contracts.

The relation of a creditor to a corporation is strictly hostile as between him and the corporation. *Earl v. Peckham*, 125 N. Y. 530, 26 N. E. 742; *Earl v. Peckham*, under a statute prohibiting conveyances and transfers by a corporation, or by a corporation in contemplation of death, to give a preference to a particular creditor or creditors, and either an actual insolvency or a contentions proved as facts, to avoid a conveyance. So long as a corporation is standing the pressure of great embarrassments, entering into the exercise of a reasonable intelligence, of going on with all of its debts, its conveyances and transfers to procure their claims, do not come within the operation of the statute. *Rev. St. U. S. §§ 5234, 5236*; *U. S. v. Aronson*, 15 N. Y. 9, 198. *Rev. St. U. S. §§ 5234, 5236*; distribution of the assets of an insolvent national bank does not invalidate liens, equities, and rights arising prior to the declaration of insolvency. In *Scott v. Armstrong*, 146 U. S. 50, a promissory note was executed to a corporation for the amount being placed to the credit of the maker, and the maker thought, and had good reason for thinking, that the managing officer of the bank knew it to be true, the charter was forfeited for insolvency, and it was held that the undrawn balance should be allowed on the note, and that such an allowance was a "preference" within the statute.

⁴⁴ Ante, p. 248.

⁴⁵ *Hi.*

tion of the contract survives, and the creditors may thus enforce their claims against any property belonging to the corporation which has not passed into the hands of bona fide purchasers.⁴⁶

SAME—CONSOLIDATION OF CORPORATIONS.

222. In most jurisdictions, where corporations are consolidated, the new corporation, in acquiring the rights and property of the old corporations, impliedly assumes their debts. It is generally so provided by statute.

It is an open question in some jurisdictions whether or not, in the absence of a statute, where corporations are consolidated the debts of the original companies follow as an incident of the consolidation, and become by implication the obligations of the new corporation; but, by the weight of authority, the question should be answered in the affirmative. The act of consolidation involves an implied assumption by the new company of all the valid debts and liabilities of the old companies. "The rule which the authorities support seems to be that where one corporation goes entirely out of existence, by being incorporated into another, if no arrangements are made respecting the property and liabilities of the corporation that ceases to exist the corporation into which it is merged will succeed to all its property, and be answerable for all its liabilities."⁴⁷

SAME—EXTENSION OF CHARTER—NEW CORPORATION.

223. If the charter of a corporation is merely extended, it remains liable, as before, for its debts. But if, when a charter is about to expire, a new corporation is created, though with the same name and

⁴⁶ Ante, p. 206; *Mumma v. Potomac Co.*, 8 Pet. 281; 1 *Cumming, Cas. Priv. Corp.* 459. And see *Smith v. Canal Co.*, 14 Pet. 45.

⁴⁷ *Louisville, N. A. & C. Ry. Co. v. Boney*, 117 Ind. 501, 20 N. E. 432. See *Indianapolis, C. & L. R. Co. v. Jones*, 29 Ind. 465; *Jeffersonville, M. & I. R. Co. v. Hendricks*, 41 Ind. 48; *Thompson v. Abbott*, 61 Mo. 176; *Mount Pleasant v. Beckwith*, 100 U. S. 514; *Pullman's Palace Car Co. v. Missouri Pac. Ry. Co.*, 115 U. S. 587, 6 Sup. Ct. 194.

the same members, it is not liable for the old, except to the extent of the liability by it from the old without consent.

We have seen, in a preceding chapter, that when a corporation is about to expire, a new corporation with the same name and the same members is formed, the new corporation is not liable for the old. It is otherwise, of course, if the existence of the corporation is merely extended, the identity of the corporation is preserved. And, as we have seen, if the stockholders of the old corporation, and transfer to it the property of the old, the transfer is fraudulent as to the creditors of the old, they may hold the new one liable to the extent of the liability received by it.⁴⁸

SAME—SET-OFF BY DEBTOR OF

224. A debtor of a corporation, who is also a creditor, may set off his claim against the corporation against other creditors. But not so as to a stockholder who is indebted to the corporation for his stock.

If a creditor of a corporation is also a stockholder, he is not liable upon his subscription by or for creditors of the corporation, but must pay his subscription ratably with other creditors in the assets.⁴⁹ In other cases. If a person who is indebted to the corporation for stock is also a creditor, he may set off his indebtedness for the benefit of his claims for losses by fire due from an insurance company set off by the assured against notes given to the corporation.

⁴⁸ *Bellows v. Hallowell*, 2 Mason, 31, Fed. Cas.

⁴⁹ *Bellows v. Hallowell*, *supra*; *President, etc., v. Bellows*, 10 Fed. Cas. 100.

⁵⁰ *Ante*, p. 549.

⁵¹ *Post*, p. 602.

⁵² *Scammon v. Kimball*, 92 U. S. 362; *Scott v. Scott*, 10 Sup. Ct. 148, *Shep. Cas. Corp.* 50.

of the company, such claim can be set off by the assured against a claim by the company for moneys deposited with him as a private banker.⁵³ A person who holds property in trust for the corporation cannot, when sued therefor after an assignment for the benefit of creditors, set off a debt due him from the corporation.⁵⁴

RELATION BETWEEN CREDITORS AND STOCKHOLDERS.

225. Stockholders are not liable at all to creditors of the corporation, at common law,

(a) Unless they are indebted to the corporation on account of their stock, and payment of the debt is necessary for the payment of creditors.

(b) Or unless the capital stock of the corporation, or a part of it, has been unlawfully distributed or paid out to them, directly or indirectly, leaving creditors unpaid.

226. In most states, constitutional provisions have been adopted, or statutes enacted, making stockholders individually liable, to a greater or less extent, for corporate debts.

One of the characteristics of a corporation, at common law, distinguishing it from a partnership, is the exemption of the members from liability for the debts of the corporation beyond the proportions of the capital stock owned by them. Partners are individually liable, as joint contractors, for all the debts of the firm, but it is otherwise with members of a corporation. If they have not paid the full amount of their subscriptions, and the corporation becomes insolvent, their liability to the corporation may be enforced by, or for the benefit of,

⁵³ *Scammon v. Kimball*, *supra*.

⁵⁴ Thus, where money is placed by a corporation in the hands of its general manager, as trustee, for safe-keeping, and to be paid out in the ordinary course of its business, he cannot set off a debt due to him by the corporation against the money in his hands, after an assignment by the corporation for the benefit of creditors. *First Nat. Bank v. E. T. Barnum Wire & Iron Works*, 58 Mich. 124, 24 N. W. 543.

creditors. But beyond the balance thus due from them to the corporation, and the amount paid in by them, they are under no liability to creditors, at common law, however insolvent the corporation may be. Creditors must look to the assets of the company, and, if the assets are insufficient to pay the debts in full, they must suffer the loss.

The only way in which liability can be imposed upon stockholders, as such, for corporate debts, is by the charter, or by statute.⁵⁵ When neither the charter of a corporation nor any general statute imposes on the individual members any personal liability to pay its debts, such liability cannot be imposed by a by-law of the corporation.⁵⁶ And the fact that individual members may have represented to the public that they were so liable will not make them liable as stockholders. If they have incurred liability as individuals disconnected with their corporate capacity, they should be proceeded against in their individual capacity, and not in their capacity as stockholders.⁵⁷

Liability on Subscriptions.

The liability of a stockholder to pay the amount of his subscription to the capital stock of the corporation is part of the capital stock, and therefore it forms a part of the assets to which creditors of the corporation are entitled to look for the payment of their debts. Whenever, therefore, a stockholder is indebted to the corporation on his subscription, the debt may be enforced by, or for the benefit of, creditors, in an appropriate action. This is well settled.⁵⁸ A corporation cannot defeat the rights of creditors to hold the stockholders liable on their unpaid subscriptions by a dissolution.⁵⁹

⁵⁵ Post, p. 564.

⁵⁶ Reid v. Manufacturing Co., 40 Ga. 98; Trustees v. Flint, 18 Metc. (Mass.) 539.

⁵⁷ Reid v. Manufacturing Co., *supra*.

⁵⁸ Hightower v. Thornton, 8 Ga. 486; Allen v. Railroad Co., 11 Ala. 487; Hatch v. Dana, 101 U. S. 205; Ogilvie v. Insurance Co., 22 How. 380; 1 Cumming, Cas. Priv. Corp. 814; Slee v. Bloom, 19 Johns. (N. Y.) 456; Briggs v. Penniman, 8 Cow. (N. Y.) 387; Bissit v. Navigation Co., 15 Fed. 353; Fehr v. Gasch (Ill.) 44 N. E. 724; Barron v. Paine, 83 Me. 312, 22 Atl. 218; Germantown Pass. Ry. Co. v. Fidler, 60 Pa. St. 124; Payne v. Bullard, 23 Miss. 88; Nevitt v. Bank, 6 Smedes & M. (Miss.) 513.

⁵⁹ Germantown Pass. Ry. Co. v. Fidler, 60 Pa. St. 124.

Conditional Subscriptions.

Where a subscription is made upon a valid condition precedent, the subscriber, as we have seen, does not become a stockholder, nor incur any liability to the corporation, until the condition is fulfilled. Nor, until then, assuming that the condition is valid, does he incur any liability on his subscription to creditors of the corporation.⁶⁰ If a conditional subscription is unauthorized and invalid, because made prior to organization under a statute requiring a certain amount of stock to be subscribed,⁶¹ it is held by some courts that the subscription is void, so that it imposes no liability either to the corporation or to creditors.⁶² Others hold that the condition only is void, and that the subscription may be treated as absolute and unconditional, so that the subscriber would be liable thereon to creditors.⁶³

It must be remembered that performance of a condition precedent may be waived. It may be waived impliedly as well as expressly, and the waiver may be relied upon by creditors. A subscriber, therefore, who waives performance of a condition by acting as a stockholder, with knowledge that it has not been performed, cannot set up the condition to defeat liability to creditors on his subscription.⁶⁴

As we have seen, there is an implied condition that the whole amount of stock specified in the charter, articles of association, or contract of subscription, or fixed by the incorporators or directors when authorized to settle the same, shall be taken by bona fide, binding, and unconditional subscriptions, before the subscribers shall be liable on their subscriptions, unless the implication is rebutted.⁶⁵ This, like other conditions, may be waived.⁶⁶

Subscriptions upon Special Terms.

We have considered subscriptions upon special terms in a preceding chapter. And we have seen that a corporation cannot make special terms with a subscriber by which it releases him from liability to pay his subscription, in whole or in part.⁶⁷ An agreement between a corporation and a subscriber by which the subscription is not to be payable, or is to be payable in part only, though it may be binding

⁶⁰ Ante, p. 294. ⁶¹ Ante, p. 312. ⁶² Ante, p. 300. ⁶³ Ante, p. 301.

⁶⁴ Ante, p. 301; Cornell's Appeal, 114 Pa. St. 153, 6 Atl. 258; Mack's Appeal (Pa. Sup.) 7 Atl. 481.

⁶⁵ Ante, p. 308.

⁶⁶ Note 64, supra.

⁶⁷ Ante, p. 302.

§§ 225-226) RELATION BETWEEN CREDITORS

upon the corporation and upon the other stockholders consenting to it, is void as against creditors of the corporation contracted with it on the faith of its capital. And the subscription may be enforced in full against the stockholders.⁶⁸

Release of Subscriber by Corporation.

A subscriber may be released, in whole or in part, by the corporation, with the consent of the stockholders, provided no claims of creditors intervene; but the amount due from him is required to pay the balance of the subscription.⁶⁹ And if a subscriber is sued by a creditor of the corporation, on his subscription, and claims that the value of his shares was reduced with the consent of the other subscribers, it is incumbent upon the corporation to show that it was done at a time when it might lawfully be done.⁷⁰

“Watered” and “Bonus” Stock.

Difficult questions arise in regard to the validity of stock issued gratuitously by the corporation where stock is issued gratuitously by which the holder pays less than its par value in money or property. We have already considered this question at length in a preceding chapter, and it is not necessary to repeat it again. We have seen that the following principles are supported by the weight of authority, though on most points there is a conflict of opinion:

(1) The transaction may be valid and binding upon the corporation and the stockholders are concerned, but it does not necessarily render it binding upon creditors.

(2) If the stock is original stock, issued or sold for less than its par value, it is a fraud upon creditors.

⁶⁸ Ante, p. 304, and cases there collected. See, per Curiam, 100 U. S. 300; Upton v. Tribilcock, 91 U. S. 45, 1 Cummings.

⁶⁹ Payne v. Bullard, 23 Miss. 88; Upton v. Tribilcock, 91 U. S. 45; Cas. Priv. Corp. 824; Slee v. Bloom, 19 Johns. (N. Y.) 411; Co. v. Badger, 67 N. Y. 294; Fehr v. Gasch (Ill.) 4 Ill. 257, and cases there cited.

⁷⁰ Payne v. Bullard, 23 Miss. 88.

who deal with it on the faith of the stock being full paid, and, if the corporation becomes insolvent, the original holders of such stock, and purchasers with notice, may be held liable for its full par value for the payment of creditors.⁷²

(3) When the corporation is an active and going concern, it may issue stock at its market value, instead of its par value, either in payment of a debt, or to raise money or purchase property necessary for carrying on its business; and if the stock is issued as full paid, and the transaction is in good faith, the holders of the stock will not be liable to creditors.⁷³

(4) If stock is issued as a bonus, and without consideration, the holders will be liable for the par value of the stock to creditors who deal with the corporation on the faith of the stock being full paid. The contrary is held in New York.⁷⁴

(5) In any case, only those creditors who have dealt with the corporation on the faith of the stock being full paid can complain. Therefore the holders of stock issued as full paid, without being paid in fact, are not liable (a) to persons who became creditors before the stock was issued, (b) or who became creditors with knowledge of the facts.⁷⁵

(6) In the absence of constitutional or statutory prohibition, stock may be paid for in property or services, if they are such as the corporation has the power to purchase or engage; and, by the weight of authority, the transaction will be valid as against creditors, if it was free from fraud, though the property may in fact have been worth less than the stock. If the overvaluation is intentional the transaction is fraudulent, as a matter of law, and obvious and gross overvaluation, if unexplained, is conclusive evidence of intentional overvaluation.⁷⁶

(7) These rules are to some extent inapplicable under peculiar constitutional or statutory provisions in force in some states.⁷⁷

Profits and Dividends.

Until dividends have been declared, the surplus profits are part of the assets of the company, and do not belong to the stockholders, even though the circumstances are such that a dividend ought to be

⁷² Ante, p. 372.

⁷³ Ante, p. 375.

⁷⁴ Ante, p. 378.

⁷⁵ Ante, p. 383.

⁷⁶ Ante, p. 379.

⁷⁷ Ante, p. 384.

declared;⁷⁸ and therefore, where a corporation has set apart its surplus profits before its surplus profits have been set apart for declaring a dividend, the surplus, as well as the profits, may be applied to satisfy its debts, to the exclusion of the claims of stockholders.⁷⁹ Where, however, while the dividend is lawfully declared, and money or property is specifically set apart as a fund appropriated to the payment of each stockholder is thereby severed from the corporation, and becomes his individual property, the claims of creditors.⁸⁰ Insolvency of the corporation has been declared and set apart does not deprive the stockholders to their shares, as against creditors.⁸¹

Diversion of Capital—Unauthorized Dividends

The directors of a corporation cannot lawfully distribute its assets required to enable the corporation to do business, by distributing it among the stockholders, or by distributing funds as dividends when there is no surplus. The whole capital stock of a corporation is not to be paid out to but bona fide purchasers, for the payment of whom the corporation has contracted on the faith of it; and it cannot be distributed among them, either directly or indirectly, among the stockholders. If it is done, the stockholders may be compelled to pay the benefit of, creditors. Such a distribution is a fraud upon creditors.⁸²

Dividends cannot lawfully be paid except out of the profits earned by the company. This is expressed in the statutes of some jurisdictions, but the rule is so even without the aid of the payment of dividends, when they cannot lawfully be paid without impair the capital stock, is a fraud upon creditors.

⁷⁸ Ante, p. 340.

⁷⁹ Scott v. Fire Co., 7 Paige (N. Y.) 198; ante, p. 340.

⁸⁰ In re Le Blanc, 14 Hun, 8, 75 N. Y. 598; Le Blanc v. Le Blanc, 14 Ch. (N. Y.) 657.

⁸¹ Id.

⁸² Wood v. Dummer, 3 Mason, 808, Fed. Cas. 805; Bartlett v. Drew, 57 N. Y. 587; Gratz v. Redd, 4 B. Mon. (Ky.) 178, 194.

⁸³ Ante, p. 344.

distribution of the capital among the stockholders, and the stockholders who receive the same may be made to account and refund for the benefit of creditors.⁸⁴ Besides this, by statute, in many jurisdictions, officers of a corporation are made liable for its debts if they pay dividends when there are no funds out of which they may lawfully be paid, and they may render themselves liable at common law.⁸⁵ But, if dividends are paid by a corporation when it may lawfully pay them, the stockholders cannot be compelled to refund, at the suit of creditors, upon the corporation's subsequently becoming insolvent.⁸⁶

Preferred Stockholders.

Ordinarily holders of preferred stock in a corporation are not to be regarded as creditors, though the stock may have been issued by the corporation for the purpose of raising money; but they are to be regarded as stockholders, and they cannot claim the right to corporate assets until the rights of creditors have been satisfied.⁸⁷ The issue of preferred stock, however, may take the form of a loan, so as to give the holders the standing of creditors.⁸⁸

SAME—STATUTORY LIABILITY OF STOCKHOLDERS.

227. In most of the states, statutes have been enacted making stockholders individually liable to some extent for corporate debts. The statutes vary in the different states. They are generally

- (a) Statutes making stockholders jointly and severally liable, absolutely and unconditionally, for all the debts of the corporation.
- (b) Statutes making them so liable until the whole capital stock is paid in, and a certificate thereof filed or recorded.
- (c) Statutes making them liable, absolutely and unconditionally, to an amount equal to the amount of

⁸⁴ Wood v. Dummer, *supra*; Bartlett v. Drew, *supra*; Main v. Mills, 6 Biss. 98, Fed. Cas. No. 8,974; Gratz v. Redd, 4 B. Mon. (Ky.) 178, 189, 191; Reid v. Manufacturing Co., 40 Ga. 98, 104; ante, p. 353.

⁸⁵ Post, pp. 605, 609.

⁸⁷ Ante, p. 365.

⁸⁶ Reid v. Manufacturing Co., 40 Ga. 98.

⁸⁸ Ante, p. 367.

§§ 227-230) RELATION BETWEEN CREDITOR

stock held by them, in addition may be due on the stock.

- (d) Statutes requiring certain accounts, filing of annual statements, and renders individuals liable for failure to comply.**

228. In a number of states there are provisions imposing individual liability on stockholders. Such provisions are designed to fix the liability, so that they require legislation to give them effect.

229. Some of the statutes impose liability as in (a), (b), and (c), supra, while that imposed by others is penal, and the nature of the contractual liability in each case upon a construction of the statute, liability may be either

- (a) In the nature of that of a surety,**
- (b) Or it may be original, as principal.**

230. In regard to the statutory liability, the following points may be pointed out:

- (a) Where a statute makes stockholders liable on dissolution of the corporation, and an assignment for the benefit of an assignee in bankruptcy or a receiver, is equivalent to a judgment.**
- (b) The words "debts," "demands," "liabilities," in a statute,
 - (1) In some states are held to include claims arising from contract,**
 - (2) In others they are held to include unliquidated damages.****
- (c) A statute making stockholders liable for "servants and laborers" for services performed by manual**

- (d) The legislature may impose individual liability upon stockholders of existing corporations, if the power to alter, amend, or repeal the charter is reserved, but not otherwise.
- (e) The legislature may repeal a statute imposing individual liability after a debt is contracted, if the liability is penal, but not if it is contractual.
- (f) The statutes have no extraterritorial operation if they are penal, but it is otherwise if they are contractual.

The statutes imposing individual liability upon stockholders for corporate debts vary so much in the different states that it is impossible to lay down general rules that will apply in all cases. There are some rules and principles, however, which are of very general application, and these may be shown, leaving the student to examine the statutes and decisions of his own state. On some questions it will be found that the courts do not agree.

The statutory liability of stockholders to creditors may be excluded by express agreement between the corporation and creditors at the time the debt is contracted.⁸⁹

Unpaid Installments of Subscriptions.

In almost all of the states, constitutional provisions have been adopted, or statutes have been enacted, expressly declaring stockholders liable for debts of the corporation to the extent of all unpaid installments on stock owned by them, or, in some states, on stock transferred by them for the purpose of defrauding creditors. Such liability exists, however, independently of any statutory provision, and has already been considered.⁹⁰ We are concerned in this section only with the liability of stockholders to creditors of the corporation which is imposed by statute, and which does not exist independently of the statute.

Unlimited Statutory Liability.

Sometimes, but not often, stockholders are made jointly and severally liable, absolutely and unconditionally, for all the debts of the corporation. Such a statute does away altogether with the common-

⁸⁹ *Brown v. Slate Co.*, 134 Mass. 590. ⁹⁰ *Ante*, p. 559.

§§ 227-230) RELATION BETWEEN CREDITORS

law exemption of members from individual debts, and, in effect, renders them liable as

Limited Statutory Liability.

More general statutes are those imposing on many states each stockholder in certain corporations liability for the debts of the corporation, "to which he is or owned by him." Such a statute creates a limited liability on the part of each stockholder, in proportion to his stock, in addition to his liability for the value of his stock, and not merely for the amount due on the stock. In such a case is, in most states, held to be correct. The stockholders are liable as principal debtors, substantially as if they were, except that the liability of each is limited to the amount of his stock.⁹¹ The national bank act makes the shareholders of every national banking association individually responsible, equally and ratably, for all contracts, debts, and engagements of the bank to the extent of the amount of their stock therein. In addition to the amount invested in such stock, if the act, it will be noticed, the shareholders are liable for the insolvency of one stockholder, or his being a defaulter. The act of the court, does not in any wise affect the liability of the bank itself, in such case, holds any of the stockholders in all respects as if such stock were in the hands of the bank to the extent of the several liability of the stockholder put up accordingly."⁹²

A stockholder is not liable at law for contracts made by the corporation without his assent, but the act making him liable to the amount of his stock.

⁹¹ See *Corning v. McCullough*, 1 N. Y. 47.

⁹² *McDonnell v. Insurance Co.*, 85 Ala. 401, 5 S. 221; *Man, 8 Cow. (N. Y.) 387*; *Root v. Sinnock*, 120 N. Y. 100; *v. White*, 14 Wis. 700; *Willis v. Mabon*, 48 Mich. 100.

⁹³ *Coleman v. White*, 14 Wis. 700.

⁹⁴ Rev. St. U. S. § 5151. The statute excepts from the liability any association then existing under state laws, having a paid up capital actually paid in, and a surplus of 20 per cent, so that they shall be liable only to the amount invested in such stock.

⁹⁵ *U. S. v. Knox*, 102 U. S. 422.

paid, on account of the debts of the corporation, a sum equal to the amount of his stock, in addition to paying for his stock, or where he is himself a creditor of the corporation to that extent.⁹⁶

Statutory Liability Until Capital is Paid in.

In a number of states, stockholders are made jointly and severally liable for debts of the corporation until the whole, or a specified proportion, of the capital stock is paid in, and a certificate thereof is made and recorded or filed as prescribed in the statute. In some states the liability is unlimited, while in others they are made liable only to the amount of their stock; that is, as we have seen, to an amount equal to the amount of their stock in addition to any amount that may have been paid or that may be due on their stock.⁹⁷ The fact that a stockholder has fully paid for his stock does not relieve him from liability, under such statutes, if the capital stock of the company, or the required proportion, is not paid in, and the certificate made and recorded or filed. Two things are necessary, under these statutes, to end the stockholders' liability. The whole capital stock, or the prescribed proportion thereof, must be paid in, and the certificate must be recorded or filed.⁹⁸ The certificate is not conclusive evidence, as against creditors, that the capital stock has been paid.⁹⁹ The question of liability under such statutes as these frequently arises in cases where stock is paid for in property, and it is claimed that the property was taken at an overvaluation. We have, in a preceding chapter, considered the effect of such payments.¹⁰⁰

If the capital stock is increased after the original stock has all been paid in, the liability of holders of the original stock, who refuse to take the new stock, is not revived under a statute making stockholders liable for the debts of the corporation until its whole capital stock is paid in, and a certificate of the fact recorded or filed. The liability in such a case rests solely upon the holders of the new stock.¹⁰¹

⁹⁶ *Garrison v. Howe*, 17 N. Y. 458; *Mathez v. Neidig*, 72 N. Y. 100; *post*, p. 603.

⁹⁷ Note 92, *supra*.

⁹⁸ *Veeder v. Mudgett*, 95 N. Y. 295.

⁹⁹ *Id.*

¹⁰⁰ *Ante*, p. 379.

¹⁰¹ *Sayles v. Brown*, 40 Fcd. 8, W. D. Smith, *Cas. Corp.* 107; *Veeder v. Mudgett*, 95 N. Y. 295.

Constitutional Provisions.

In a number of states there are constitutional provisions making stockholders liable, to a greater or less extent, for the debts of the corporation. Whether these provisions are self-executing or they require statutory enactment to carry them into effect, upon a construction of the language of the provision. In *Mitchell* in a Minnesota case, the nature and effect of the provision posed is fixed by the provision itself, so that upon an examination and construction of its own language used indicating that the subject-matter is for action, the provision should be construed in accordance with its language as addressed to the courts. In a constitutional provision that "each stockholder * * * [with certain exceptions] shall be liable for the debts of the stock held or owned by him" was self-executing. On the other hand, the provision leaves anything to be fixed by the legislature, given effect, or if, on a construction of the provision in the light of other provisions bearing upon the same, it appears that it is addressed to the legislature, and the provision cannot be regarded as self-executing.

Effect of Dissolution of Corporation.

The dissolution of a corporation by its own act or by a court, or by ceasing to act as a corporation, does not discharge the stockholders from their liability to creditors to enforce the statutory liability of stockholders.

Nature of Stockholders' Liability—Penal.

The liability of stockholders under some statutes is civil, while under others it is penal. This distinction is important. For instance, penal statutes have no extrajurisdictional effect. Liability for a penalty does not survive the death of the person liable. The effect of the statute, and not the form, determines the nature of the liability. A statute which directs or prohibits some act is penal.

¹⁰² *Willis v. Mabon*, 48 Minn. 140, 50 N. W. 102. The fact that a remedy is provided for does not show that the provision is civil. If a liability being imposed, the law furnishes a remedy.

¹⁰³ *French v. Teschemaker*, 24 Cal. 518; *Morley v. Frankland*, 10 Q. B. 542.

¹⁰⁴ *Sleeper v. Goodwin*, 67 Wis. 577, 31 N. W. 577, 59 N. Y. 548.

¹⁰⁵ *Diversey v. Smith*, 103 Ill. 378.

feiture for its transgression, is a penal statute. Therefore a statute providing that a corporation shall not transact business until certain preliminaries have been complied with, and that, if it does, the members shall be personally liable to the creditors, has been held to impose a penalty.¹⁰⁶ So, where the corporation is required to file annually a certificate setting forth certain facts, such as the amount of assessments voted by the company and actually paid in, and the amount of all existing debts, and it is provided that, if it shall fail to do so, all the stockholders shall be jointly and severally liable for all the debts of the company, the liability thus imposed is penal, and not contractual.¹⁰⁷

But the liability under a statute providing that all stockholders shall be severally or jointly and severally liable individually to the creditors of the corporation, to an amount equal to the amount of their stock, for all debts or contracts made by the company, until the whole amount of the capital stock shall have been paid in, and a certificate thereof filed, is not in the nature of a penalty, but a liability arising upon a contract.¹⁰⁸ The same is true of a statute making stockholders liable, absolutely and unconditionally, for the debts of the corporation, or liable to the extent of their stock, as in the national banking act.¹⁰⁹

Same—Nature of Contractual Liability.

The statutory or constitutional liability of stockholders *ex contractu* for corporate debts to the amount of their stock, though *sui generis*, is in some cases, but not in all, in the nature of the liability of a surety or guarantor.¹¹⁰ Sometimes it is said to be that of a

¹⁰⁶ *Id.*

¹⁰⁷ *Sayles v. Brown*, 40 Fed. 8, W. D. Smith, Cas. Corp. 107; *Wing v. Slater* (R. I.) 35 Atl. 302.

¹⁰⁸ *Flash v. Conn.*, 109 U. S. 371, 3 Sup. Ct. 263; *Id.*, 16 Fla. 428, 26 Am. Rep. 721; *Cuykendall v. Miles*, 10 Fed. 342.

¹⁰⁹ *Richmond v. Irons*, 121 U. S. 27, 7 Sup. Ct. 788; *Cochran v. Wiechers*, 119 N. Y. 399, 23 N. E. 803; *Grand Rapids Sav. Bank v. Warren*, 52 Mich. 557, 18 N. W. 356; *Corning v. McCullough*, 1 N. Y. 47; *Queenan v. Palmer*, 117 Ill. 619, 7 N. E. 613; *Hencke v. Twomey*, 58 Minn. 550, 60 N. W. 667, W. D. Smith, Cas. Corp. 106.

¹¹⁰ *Willis v. Mabon*, 48 Minn. 140, 50 N. W. 1110. It was therefore held in this case that the insolvent law, providing that the release of any debtor under the act should not discharge "any other party liable as surety, guarantor, or

§§ 227-230) RELATION BETWEEN CREDITORS

guarantor or surety or partner,¹¹¹ but it is far. In some respects it is similar, but in ent.¹¹² "The truth is," says Mr. Taylor, "that under statutes imposing individual liability, the liability of shareholders under such statutes is not as the liability of guarantors, or the call it what it is not."¹¹³ The nature of the liability is upon the particular statute. It may be in the case of a surety or guarantor, or it may not. In the case of a bank provided that the persons and property of the bank should be "at all times liable, pledged and secured by all of the bills and notes of the bank, at any time," the number of shares that each individual owned, it was held that the stockholders were liable for the bills of the bank at their face, after they had been paid to the bank and payment refused, although the stockholder had assets in his hands sufficient to pay the debt. The statute making stockholders, upon default of payment of any debt, individually responsible, and individually liable for an amount equal to the value of their shares, it has been held that the liability of the stockholders is

otherwise for the same debt," included stockholders' debts of the corporation. See, also, *National Loan and Trust Co. v. Walner*, 100 Pa. St. 100, 45 Am. Rep. 359.

¹¹¹ *Hanson v. Donkersley*, 37 Mich. 184. But see *Warren v. Bank*, 52 Mich. 557, 18 N. W. 358.

¹¹² *In Grand Rapids Sav. Bank v. Warren*, see *Justice Cooley*: "The shareholder, it is true, occupies the position of surety for the bank [citing *Hansen v. Bank*], but he is something more than a surety; he is one of the members of the bank. Under the very terms of the association, he is deemed to be bound by the bank contracts."

¹¹³ *Taylor v. Corp.* § 714.

¹¹⁴ *Hatch v. Burroughs*, 1 Woods, 439, Fed. C. 123; *Hyman v. McCullough*, 2 Denio (N. Y.) 123; *Parrott v. Colby*, 6 Hun (N. Y.) 57, 71 N. Y. 521. An extension of the debt by the stockholders' consent, does not release them from the liability of one who was strictly a surety or guarantor. *See* *Walker v. Walker*, 76 N. Y. 521. An extension of the debt by the stockholders' consent, does not release them from the liability of one who was strictly a surety or guarantor. (*Mass.*) 569.

the same as the liability of partners, except that, in the latter case, they are only liable to the amount of their stock.¹¹⁵

The liability under a statute making stockholders liable for corporate debts until the capital stock is paid in, and a certificate thereof filed, has been held to be unconditional, original, and immediate, and not collateral to the liability of the corporation, nor in any degree dependent upon the insufficiency of the corporate assets.¹¹⁶

What Constitutes "Dissolution."

A statute making stockholders liable for debts of the corporation at the time of its dissolution does not mean a dissolution by expiration of the charter, or by action of the state. A dissolution, so as to render stockholders liable under the statute, is effected by its total insolvency, and the appointment of a receiver, or an assignee in bankruptcy or insolvency, to take charge of its property and wind up its business, or an assignment for the benefit of creditors, and suspension of business.¹¹⁷

But a right of action does not accrue against stockholders upon the corporation becoming insolvent in the sense, simply, that its property is insufficient for the payment of its debts, nor upon the appointment of a receiver merely for the purpose of carrying on its business, and not account of its insolvency, or to wind up its business.¹¹⁸

"Debts," "Demands," etc., within the Statutes.

There is some difference of opinion in the construction of the word "debts" or "demands" or "dues," used in the statutes under consideration. It has been held that the term "debt" does not include unliquidated claims for damages for torts of the corporation, for which no judgment has been recovered, but is intended to include only "those obligations arising on express and implied contracts, growing out of dealings between the corporation and other corporations or individ-

¹¹⁵ Schalucky v. Field, 124 Ill. 617, 16 N. E. 904; Thompson v. Meisser, 108 Ill. 359; Fuller v. Ledden, 87 Ill. 310; Corning v. McCullough, 1 N. Y. 47.

¹¹⁶ Manufacturing Co. v. Bradley, 105 U. S. 175.

¹¹⁷ Slee v. Bloom, 19 Johns. (N. Y.) 456; Briggs v. Penniman, 8 Cow. (N. Y.) 387; McDonnell v. Insurance Co., 85 Ala. 401, 5 South. 120; Barrick v. Gifford, 47 Ohio St. 180, 24 N. E. 259; Bronson v. Schneider, 49 Ohio St. 438, 33 N. E. 233; Younglove v. Lime Co., 49 Ohio St. 663, 33 N. E. 234.

¹¹⁸ Bronson v. Schneider, *supra*; Younglove v. Lime Co., *supra*.

§§ 227-230) RELATION BETWEEN CREDITORS

uals, where the financial condition of such co be the foundation of credit." ¹¹⁹ Some cour statutes cover a demand for unliquidated tort. ¹²⁰ A judgment for a tort is an "indebt ing of a statute." ¹²¹

The statutory liability of members of a co tends to debts contracted in another state. debts to the same extent as for debts contr

Debts Due Clerks, Laborers, etc.

In some states a liability is imposed by for debts due clerks, servants, and laborers the corporation. Of course, the statutes va A foreman or superintendent who is not an but an employé, has been held a servant, statute making stockholders liable for debts laborers for services," though he does not But a bookkeeper employed at a yearly s within a statute imposing liability for debts apprentice," as it was considered that the include only persons performing menial or n ices of that class of persons who look to th for present support, from whom the compa and to whom its future ability to pay is has also been held that a traveling salesma the meaning of such statutes. ¹²⁵

¹¹⁹ Doolittle v. Marsh, 11 Neb. 243, 9 N. W. 5 "demands," in a New York statute, did not inclu son of a bridge of the corporation being out of rep Wend. (N. Y.) 58. So in Massachusetts it has b infringement of letters patent is not, before judgm making officers liable. Child v. Iron Works, 137

¹²⁰ Rider v. Fritchey, 49 Ohio St. 285, 30 N. E. word "dues." Carver v. Manufacturing Co., 2 St

¹²¹ Powell v. Railway Co., 36 Fed. 726.

¹²² Hutchins v. Mining Co., 4 Allen (Mass.) 580

¹²³ Sleeper v. Goodwin, 67 Wis. 577, 31 N. W. 55 Wis. 465, 13 N. W. 452.

¹²⁴ Wakefield v. Fargo, 90 N. Y. 213.

¹²⁵ Jones v. Avery, 50 Mich. 326, 15 N. W. 49

Excepted Classes of Corporations.

Sometimes the statutes except certain corporations from their operation. Thus, Minnesota corporations organized for the purpose of carrying on any kind of manufacturing or mechanical business are excepted. To come within such an exception a corporation must have been organized exclusively for carrying on a manufacturing or mechanical business. If the purpose for which a corporation is formed, as stated in its articles of association, is to carry on a manufacturing or mechanical business, and also some other and distinct kind of business, not properly incidental to or connected with the former, it will not be within the exception.¹²⁶

Release or Discharge of Corporation.

Where the statute makes stockholders liable for the debts and contracts of the corporation jointly with the corporation, there must be a debt due from the corporation, to render a stockholder liable. If a creditor of the corporation, therefore, releases the corporation from the debt, in insolvency proceedings or otherwise, there is no longer any debt upon which he may hold the stockholders. The liability of the stockholders is in the nature of the liability of partners for a debt of the firm, and whatever releases the corporation releases them also.¹²⁷

Constitutional Law—Laws Affecting Existing Corporations.

If the legislature has reserved the right to amend, alter, or repeal the charter of a corporation, it may, by a law passed after incorporation, impose individual liability upon the stockholders for corporate debts.¹²⁸ And it has been held that it can do so even where the power of alteration, amendment, or repeal has not been reserved; that such a law is not unconstitutional as impairing the obligation of the contract between the stockholders and the state as evidenced by the charter.¹²⁹

¹²⁶ State v. Minnesota Thresher-Manuf'g Co., 40 Minn. 213, 41 N. W. 1020; Mohr v. Elevator Co., 40 Minn. 343, 41 N. W. 1074; Arthur v. Willius, 44 Minn. 409, 46 N. W. 851; Densmore v. Shepard, 46 Minn. 54, 48 N. W. 528.

¹²⁷ Mohr v. Elevator Co., 40 Minn. 343, 41 N. W. 1074.

¹²⁸ Ante, p. 216; Sleeper v. Goodwin, 67 Wis. 577, 31 N. W. 335.

¹²⁹ Ante, p. 210, note; Gray v. Coffin, 9 Cush. (Mass.) 192.

Same—Repeal or Change of Law.

It has been generally held that, where the stockholders for debts and contracts of the corporation are within the protection of the clause of the federal laws impairing the obligation of contracts, where a statute or the charter of a corporation limits the stockholders liability for the debts of the corporation to the value of their stock, an act or constitutional provision amending the charter so as to take away this protection is unconstitutional and void as to existing creditors.¹⁸⁰ It is, however, to the contrary.¹⁸¹ Certainly the form of remedy for enforcing the liability

Extraterritorial Effect of Statutes.

If the statute imposing liability on stockholders of a corporation is penal, it has no operation in another state, for penal statutes have no extraterritorial effect. In a Rhode Island statute requiring a corporation to file a certificate setting forth the amount of assessments levied and actually paid in, and the amount of the unpaid assessments, that, if it should fail to do so, all the stockholders are jointly and severally liable for all the debts of the corporation, the statute, being penal, imposed no liability enforceable against stockholders in Maryland.¹⁸²

If, on the other hand, the liability is contractual, the liability for corporate debts is imposed until the contract may be enforced in another state by any court having jurisdiction of the subject-matter and the parties.¹⁸⁴

¹⁸⁰ *Hathorne v. Calef*, 2 Wall. 10; *Grand Rapids v. Michigan*, 557, 18 N. W. 356; *McDonnell v. Insurance Co.*, 120.

¹⁸¹ *Coffin v. Rich*, 45 Me. 507, 71 Am. Dec. 559.

¹⁸² *Fourth Nat. Bank v. Francklyn*, 120 U. S. 71.

¹⁸³ *Sayles v. Brown*, 40 Fed. 8, W. D. Smith, C. C. v. McLean, 12 Allen (Mass.) 438.

¹⁸⁴ *Flash v. Conn.*, 109 U. S. 371, 3 Sup. Ct. 217; *Cuykendall v. Miles*, 10 Fed. 342.

SAME—WHO ARE LIABLE AS STOCKHOLDERS UNDER THE STATUTES.

231. Those who appear on the books of the corporation are *prima facie* liable under the statutes as stockholders. But there are some exceptions:

- (a) A person is not liable if stock is registered in his name, without his knowledge or consent, express or implied.
- (b) As to the effect of a transfer of shares, the authorities are conflicting:
 - (1) In some states the transferror is relieved from liability, and the transferee takes his place.
 - (2) In others, the transferror remains liable for debts contracted while he was owner of the shares, and no liability therefor attaches to the transferee.
 - (3) In others, both are liable for debts contracted while the transferror owned the shares.
 - (4) Generally this question is settled by the express terms of the statute.
 - (5) Where the shares are transferable on the books of the corporation a transferror is not relieved from liability unless he has his transfer registered, or takes due steps to have it done.
 - (6) A transfer to a person who is incapable of holding the stock and of assuming liability in respect thereto does not relieve the transferror from liability.
 - (7) Nor is he relieved by a transfer to an insolvent person for the purpose of escaping liability, when he knows the corporation to be insolvent.
 - (8) Nor is he relieved by a colorable transfer.
 - (9) Nor is he relieved by a transfer after the corporation has become insolvent and ceased to do business.

- (10) Where stock transferable on the books of the corporation is transferred to a pledgee, trustee, etc., he is personally liable thereon if he appears on the books as the absolute owner, but not otherwise.
- (11) Creditors must elect whether to hold the real or the apparent owner. They cannot hold both.
- (c) Married women, if capable of holding stock, are subject to the statutory liability, though they may not have capacity to contract, as the liability is imposed by statute.
- (d) The statutory liability survives, as against the personal representative of a deceased stockholder, if the liability is contractual, but not if it is penal.
- (e) Forfeiture of stock for nonpayment of assessments releases the stockholder from statutory liability, if he thereby ceases to be a stockholder.
- (f) Holders of certificates of unauthorized stock are not liable unless the circumstances estop them as against creditors.

Where the statute makes stock transferable on the books of the corporation, and makes "shareholders" or "stockholders" liable for the debts of the corporation,¹⁸⁵ the general rule is that every person in whose name, as owner, stock is registered on the books of the corporation, with his knowledge and consent, is liable. He is a "shareholder" or "stockholder," within the meaning of the statutes. When the name of an individual appears on the stock book of a corporation as a stockholder, the presumption is that he is the owner of the stock, and, in an action against him as stockholder, he has the burden of rebutting the presumption.¹⁸⁶ To this rule there are some exceptions. These will be pointed out as we go along.

¹⁸⁵ Ante, p. 564, where some of the statutes are given.

¹⁸⁶ *Turnbull v. Payson*, 95 U. S. 418.

Shares Registered in Name of Person without His Knowledge.

It is clear that a person cannot be compelled to become a stockholder, and to assume liability as such, without his consent. Membership in a corporation can only result from contract, express or implied, and there can be no contract without mutual consent. It follows that, if shares in a corporation are registered in the name of a person without his knowledge or consent, he cannot be held liable.¹³⁷ He may become liable, however, by acquiescence after knowledge of the facts, for consent in such a case will be implied.¹³⁸ And if a person is elected to an office in the corporation for which ownership of stock is a necessary qualification, and shares are transferred to him on the books, and he acts as such officer, he will be chargeable with knowledge of the fact that shares stand in his name.¹³⁹

Effect of Transfer of Shares.

In *President, Directors, etc., of Middletown Bank v. Magill*,¹⁴⁰ under a charter declaring that members of a corporation should at all times be liable for all debts due by the corporation, it was contended by the plaintiffs, and held by two of the judges, that the legislature intended to subject members to the same liability as if they had not been incorporated,—that is, to the liability of partners,—and that members of the corporation at the time a debt was contracted became subject to a liability therefor, which continued notwithstanding a valid sale and transfer of their shares, and that transferees became liable only for debts contracted after the transfer. A majority of the court, however, held that no liability attaches under such a statute

¹³⁷ *Stephens v. Follett*, 43 Fed. 842. In this case it was held that a person who had subscribed and paid for a specified number of shares of a "proposed increase" of the capital stock of a national bank was not liable as a shareholder, where the increase was never in fact issued, but the bank officials transferred to him instead, on the books of the bank, old stock of the bank, without his consent or knowledge. It was further held that he was not estopped to deny that he was a shareholder by the fact that he received a dividend on the old shares so transferred to him, where he received it in the belief that it was paid him by virtue of his subscription to the new stock. And see *Simmons v. Hill*, 96 Mo. 679, 10 S. W. 61.

¹³⁸ *Keyser v. Hitz*, 133 U. S. 138, 10 Sup. Ct. 290; *Finn v. Brown*, 142 U. S. 56, 12 Sup. Ct. 136.

¹³⁹ *Finn v. Brown*, *supra*.

¹⁴⁰ 5 Conn. 28, 1 Cumming, Cas. Priv. Corp. 912.

until the corporate property fails, and to the stockholders' liability; and, the such persons only, as are then stockholders, and that a valid and complete transfer of express charter or statutory provisions of transferror of all liability to creditors by statutes, and the transferee becomes liable.

On this point the decisions in the cases are clearly, a valid transfer relieves the transferee of liability subsequently contracted.¹⁴¹ In most cases it is held that the transferee of shares is liable for the debts acquired the shares if he holds them when the liability is enforced.¹⁴² But he is not liable if the liability is sought to be enforced when the transferror of shares is relieved of liability contracted while he was a stockholder, if he transfers the shares. But others hold, without qualification, that the transferee of stock, while some hold that he is liable for the debts of the corporation or for any other reason the liability cannot be enforced though the transfer was bona fide.¹⁴³ It was held that the liability under a statute for the debts of the corporation until the

¹⁴¹ *Chemical Nat. Bank v. Colwell*, 132 N. Y.

¹⁴² *Curtis v. Harlow*, 12 Metc. (Mass.) 8; 667; *Barrick v. Gifford*, 47 Ohio St. 180, 24 Ill. 350, 11 N. E. 339; *Sayles v. Bates*, 15 R. I. 342, 5 Atl. 49; *Brown*, 24 Vt. 197; *National Commercial Bank v. South*, 149. Contra, *Chesley v. Pierce*, 32 N. Y. Corp. 936; *Moss v. Oakley*, 2 Hill (N. Y.) 265; (N. Y.) 567.

¹⁴³ *Sayles v. Bates*, 15 R. I. 342, 5 Atl. 49; *Cush*, (Mass.) 183.

¹⁴⁴ *Dauchy v. Brown*, 24 Vt. 197; *Bond v. Middleton Bank v. Magill*, 5 Conn. 912. But see *Curtis v. Harlow*, 12 Metc. (N. Y.) 567.

¹⁴⁵ *Moss v. Oakley*, 2 Hill (N. Y.) 265; *Brady v. Mason v. Alexander*, 44 Ohio St. 318, 7 N. E. St. 397, 21 N. E. 637; *Sayles v. Bates*, 15 R. I. 342, 5 Atl. 49; *Meek*, 87 Tenn. 69, 9 S. W. 225; *Holyoke*, 183; *Johnson v. Bleaching Co.*, 15 Gray (Ma

a certificate thereof recorded, includes all persons who were stockholders when the debt was contracted, and all persons who are stockholders when the liability is sought to be enforced, but does not extend to persons becoming stockholders after the debt was contracted, and ceasing to be such before the debt becomes payable and action is brought.¹⁴⁶ And such seems to be the rule in Massachusetts.¹⁴⁷

Sometimes the statute, as is the case with the national banking act, expressly declares that transferees of stock shall succeed to the liabilities of the transferror. In such a case there can be no doubt that a valid and complete transfer relieves the transferror of liability, and substitutes the transferee in his place.¹⁴⁸

Same—Registration of Transfer.

Where, by the charter, or by statute, shares are transferable on the books of the corporation, the rule is that the person who appears on the books as owner is the one to whom the statutory liability attaches. In order, therefore, that a shareholder may relieve himself from liability, even by an actual and bona fide sale of his stock, he must take all due precautions to have the transfer properly registered. Thus, where a shareholder in a national bank had sold his stock several months before the insolvency of the bank, but the transfer was not registered on the books until the date of the bank's failure, and it did not appear that any steps were taken by him to have it registered, he was held subject to the statutory liability.¹⁴⁹ But the vendee of shares, who fails to have the transfer registered, will be liable to the vendor for anything which the latter may be compelled to pay by reason of his appearing on the books as the owner of the shares.¹⁵⁰

A shareholder who has sold his stock will not be liable merely because the transfer has not been made on the books, where he is not

¹⁴⁶ Sayles v. Bates, *supra*.

¹⁴⁷ Holyoke Bank v. Burnham, *supra*.

¹⁴⁸ Johnson v. Laffin, 5 Dill. 65, Fed. Cas. No. 7,393, 1 Cumming, Cas. Priv. Corp. 608; *Id.*, 103 U. S. 800; Whitney v. Butler, 118 U. S. 655, 7 Sup. Ct. 61; Cleveland v. Burnham, 55 Wis. 598, 13 N. W. 677.

¹⁴⁹ Richmond v. Irons, 121 U. S. 27, 7 Sup. Ct. 788; Price v. Whitney, 28 Fed. 297; Irons v. Bank, 27 Fed. 591; Johnson v. Bleaching Co., 15 Gray (Mass.) 216. But see, *contra*, Harpold v. Stobart, 46 Ohio St. 397, 21 N. E. 637.

¹⁵⁰ Johnson v. Underhill, 52 N. Y. 202.

in any way to blame for such omission that he has done all that a careful & reasonably do to effect a transfer of liable.¹⁵¹

Same—Transfer to Person Incapable

The transfer, to relieve the transferor to some one who is capable in law of and of assuming the transferor's liability.

Same—Transfer to Infant.

Thus, a transfer to an infant, even if it does not relieve the transferor from liability, if he has attained his majority, and become himself a transferor.

Same—Transfer to Corporation.

As has been shown, it is the general principle that a corporation has the power to deal in its own stock. The Supreme Court declares that national banking associations may purchase or transfer of shares to the corporation itself, at least, if not expressly prohibited, unless it is to the corporation itself, or to a known agent, or to change the relation of the parties, and to release the transferor from liability as a stockholder for the shares. But it has been held that a corporation may purchase and hold shares in another corporation as a stockholder, notwithstanding the ultra vires doctrine.¹⁵⁵ If a stockholder acts in good

¹⁵¹ Whitney v. Butler, 118 U. S. 655, 7 Sup. Ct. 894; Hayes v. Shoemaker, 39 Fed. 319; Chicago v. Y. 250, 30 N. E. 644.

¹⁵² Nickalls v. Merry, L. R. 7 H. L. 530; Weston's Case, 5 Ch. App. 614, 620.

¹⁵³ Mann's Case, 3 Ch. App. 459, note, 1 Ct. App. 1, cited in preceding note.

¹⁵⁴ Johnson v. Laffin, 5 Dill. 65, Fed. Cas. 608; Id., 103 U. S. 800.

¹⁵⁵ Citizens' State Bank v. Hawkins, 18 Ct. App. 1, based on the principle that "the doctrine of ultra vires, for or against a corporation, should not be applied so as to defeat the ends of justice, and work a legal wrong."

though it may be to the president of the corporation, not knowing that the purchase is really on behalf of the corporation, the transfer is valid, and he ceases to be a stockholder for any purpose; but in such a case the president or other person becomes the real transferee, in his individual capacity, and is substituted for the transferror, and he becomes liable on the shares as a stockholder.¹⁵⁶

Same—Transfer to Insolvent.

In this country it is generally held that a stockholder who knows that the corporation is insolvent cannot transfer his shares to an irresponsible or insolvent person, for the purpose of escaping liability to creditors of the corporation. In such a case the transfer is void as to the creditors, and the transferror remains liable. And it makes no difference that the transfer is "out and out," so as to divest the transferror of all interest therein.¹⁵⁷ In England the rule is different. It is there held that a stockholder may sell and transfer his shares to an insolvent person, or man of straw, and if the transaction is a bona fide, "out and out" sale and transfer, he cannot be held liable to creditors, even though his motive was to escape liability.¹⁵⁸

It has been held that a sale by a pledgee of stock, pursuant to a power of sale in his contract, is not voidable, as a fraud on creditors of the corporation, though made to an insolvent person for the purpose of escaping liability.¹⁵⁹

In the absence of actual fraudulent intent, the fact that the transferee was insolvent will not prevent the transfer from being effectual so as to release the transferror from further liability as a stockholder, though knowledge of insolvency would be strong evidence of fraud.¹⁶⁰

Same—Sham or Colorable Transfers.

Not only in this country, but in England as well, it is settled law that in case of a transfer to an insolvent or irresponsible person, if

¹⁵⁶ Johnson v. Laffin, *supra*.

¹⁵⁷ Marcy v. Clark, 17 Mass. 330; Nathan v. Whitlock, 3 Edw. Ch. (N. Y.) 215, 1 Cumming, Cas. Priv. Corp. 953; Bowden v. Johnson, 107 U. S. 251, 2 Sup. Ct. 246; Dauchy v. Brown, 24 Vt. 197. But see Chouteau Spring Co. v. Harris, 20 Mo. 383.

¹⁵⁸ De Pass' Case, 4 De Gex & J. 544.

¹⁵⁹ Holyoke Bank v. Burnham, 11 Cush. (Mass.) 187; Magruder v. Colston, 44 Md. 349.

¹⁶⁰ Miller v. Insurance Co., 50 Mo. 55.

§ 231) RELATION BETWEEN CREDITORS

the transaction is not a bona fide, "ou but a mere simulation to avoid appearing error will remain liable. Stockholder liability by thus transferring the share or some other irresponsible party. But the actual owners of stock cannot shield by thus putting the title to the stock in person. "Creditors have the right to cers for contribution, and this right cannot orable transfer of the legal title to some the same for the benefit of the real own

The same is true where a man buys tered on the books of the corporation in person, without its ever having appeared name. In such a case the creditors of liable.¹⁶¹

Same—Transfer after Suspension of

It has been held that after a nation and has closed its doors and stopped d shareholders to creditors is so far fixe their shares will be held fraudulent and creditors.¹⁶² And the same may be said

Pledgees.

It is well settled, where stock is transferred to a corporation, that, if stock in a corporation is transferred to a person in such a way that he appears on the books as the sole owner, the creditors of the corporation are entitled to look behind the books and inquire into equity between him and the corporation, or between him and the person to whom he took the transfer. If he appears on the books as the real owner, he is, as far as the rights of

¹⁶¹ Welles v. Larrabee, 36 Fed. 866, 868. S. 75, 1 Cumming, Cas. Priv. Corp. 944; Williams v. National Bank v. Case, 99 U. S. 628, 1 Cum. v. Stevens, 17 Blatchf. 259, Fed. Cas. No. 3,6

¹⁶² Davis v. Stevens, 17 Blatchf. 259, Fed.

¹⁶³ Irons v. Bank, 17 Fed. 308.

cerned, a stockholder, and subject to the statutory liability, though he may in fact hold the stock merely as collateral security.¹⁶⁴ The chief reason for this rule is that the pledgee, by thus taking the absolute legal title, and holding himself out as the legal owner of the stock, estops himself from setting up the fact that he was merely a pledgee. "The true ground of liability, where it exists, is not because the pledgee is the owner in fact of the stock, for he is not, but the fact that the pledgee has received a transfer of the stock in such form that the legal ownership appears to be in him; and, by thus holding himself out as apparent owner, he is estopped from showing the contrary."¹⁶⁵ The rule ceases when the reason ceases. Therefore, if there is anything on the stock books of the corporation showing that the transferee takes as pledgee, he incurs no liability.¹⁶⁶ As was said by the supreme court of the United States, "It has never, to our knowledge, been held that a mere pledgee of stock is chargeable, where he is not registered as owner."¹⁶⁷ A pledgee, for instance, is not liable if the stock stands in his name on the books "as pledgee," or if it expressly appears to be held "as collateral."¹⁶⁸

¹⁶⁴ *National Bank v. Case*, 99 U. S. 628, 1 Cumming, Cas. Priv. Corp. 948; *Wheelock v. Kost*, 77 Ill. 296; *Aultman's Appeal*, 98 Pa. St. 516; *Adderly v. Storm*, 6 Hill (N. Y.) 624; *Rosevelt v. Brown*, 11 N. Y. 148; *United States Trust Co. v. United States Fire Ins. Co.*, 18 N. Y. 199; *National Commercial Bank v. McDonnell*, 92 Ala. 387, 9 South. 149; *Magruder v. Colston*, 44 Md. 349; *Holyoke Bank v. Burnham*, 11 Cush. (Mass.) 183; *Crease v. Babcock*, 10 Metc. (Mass.) 525; *First Nat. Bank v. Hingham Manuf'g Co.*, 127 Mass. 563; *Hale v. Walker*, 31 Iowa, 344; *Sleeper v. Goodwin*, 67 Wis. 577, 31 N. W. 335; *Hoare's Case*, 2 Johns. & H. 229; *Moore v. Jones*, 3 Woods, 53, Fed. Cas. No. 9,769; note, 15 C. C. A. 133, 134. "It is now too well settled to be any longer a question that when stock is transferred to a man as collateral, and stands in his name, he incurs liability as a stockholder just as if he were the actual beneficial owner. Most especially is this just and right as to creditors who trust to his name, and have no notice of the secret trust upon which the stock is held." *Aultman's Appeal*, supra.

¹⁶⁵ *Welles v. Larrabee*, 36 Fed. 866.

¹⁶⁶ *Anderson v. Warehouse Co.*, 111 U. S. 479, 4 Sup. Ct. 525; *Beal v. Bank*, 15 C. C. A. 128, 67 Fed. 816; *Pauly v. Trust Co.*, 56 Fed. 430, affirmed 7 C. C. A. 422, 58 Fed. 666; *Welles v. Larrabee*, 36 Fed. 866; *Henkle v. Manufacturing Co.*, 39 Ohio St. 547; *First Nat. Bank v. Hingham Manuf'g Co.*, 127 Mass. 563; note, 15 C. C. A. 134. But see *Grew v. Breed*, 10 Metc (Mass.) 569.

¹⁶⁷ *Anderson v. Warehouse Co.*, supra.

¹⁶⁸ See cases in note 166, supra.

Under a statute rendering stockholders personally liable but providing that no person holding stock shall be considered as holding the stock if the pledgee of shares cannot be held liable it has also been held that this is true with the corporation itself as collateral.¹⁷⁰

Trustees, Executors, Agents, etc.

The same doctrine applies, in the absence of a statute, where stock is held in trust. A trustee of the books of the corporation as the absolute owner is personally liable to the creditors of the corporation. If he in fact holds the stock as trustee, personally liable, etc.¹⁷¹ But, by the weight of authority, a trustee holding, not in his own right, but as "trustee," will not be personally liable.¹⁷² Of course, in his representative capacity, to the extent of the assets, sometimes expressly provided by statute as executors, trustees, etc., shall not be personally liable as stockholders, but that the estate shall be liable.¹⁷⁴

A broker or other agent who purchases stock for a company who takes the title in his own name, on behalf of the company, is liable as a stockholder.¹⁷⁵

¹⁶⁹ *McMahon v. Macy*, 51 N. Y. 155; *Union Sav. Ass'n v. Seligman*, 15 S. W. 630; *Burgess v. Seligman*, 107 U. S. 379; *Albert v. Seligman*, 24 Md. 527.

¹⁷⁰ *Union Sav. Ass'n v. Seligman*, supra; *Burgess v. Seligman*, supra.

¹⁷¹ See *Adderly v. Storm*, 6 Hill (N. Y.) 624; *Crease v. Babcock*, 10 Metc. (Mass.) 525, 545; *States Trust Co. v. United States Fire Ins. Co.*,

¹⁷² *Welles v. Larrabee*, 38 Fed. 866; dictum in *Welles v. Larrabee*, 38 Fed. 868. Contra, *Grew v. Breed*, 10 Metc. (Mass.) 525.

¹⁷³ See *Richmond v. Irons*, 121 U. S. 27, 7 R. I. 342, 5 Atl. 407.

¹⁷⁴ There is such a provision in the national

¹⁷⁵ *McKim v. Glenn*, 66 Md. 479, 8 Atl. 130.

Election between Apparent and Real Owner.

Where the person who appears on the books of the corporation as the owner of stock is not the real owner, creditors cannot hold both him and the real owner to the statutory liability; nor can they hold one of them after an unsuccessful attempt, with knowledge of the facts, to hold the other. They must elect between them. Thus, it was held that a person who was entered on the books of a national bank as the owner of stock, but who was admitted to hold the stock in trust for the real owner, could not be held liable to creditors of the bank after the real owner had been proceeded against to judgment, though nothing was realized upon the judgment.¹⁷⁶

Assignees in Bankruptcy or Insolvency.

The assignees in bankruptcy or insolvency of a stockholder are not subject to the statutory liability of the bankrupt or assignor for debts of the corporation.¹⁷⁷ It has been so held even where the assignee had attended and voted at meetings of the corporation, and done other acts of ownership of the stock.¹⁷⁸

Married Women.

Where a married woman is not only capable of holding stock in a corporation, but is also, by statute, capable of contracting as a feme sole, it is clear enough that she may be held liable as a shareholder to the creditors of a corporation. The question is not so clear, however, in those jurisdictions where the common-law disability of married women to contract has not been wholly removed. In the federal courts it is held that, where a married woman is capable of holding stock in a corporation, she may be held liable, as a shareholder in a national bank, for the contracts and debts of the bank, even though, by the law of the particular jurisdiction, she may not have the capacity to contract. The reason that she may be held is that her liability is imposed by the statute, and does not rest upon contract.¹⁷⁹ The same rule must apply to other corporations.

¹⁷⁶ *Yardley v. Wilgus*, 56 Fed. 965.

¹⁷⁷ *American Fife Co. v. Garrett*, 110 U. S. 288, 4 Sup. Ct. 90; *Gray v. Coffin*, 9 Cush. (Mass.) 192.

¹⁷⁸ *Gray v. Coffin*, 9 Cush. (Mass.) 192.

¹⁷⁹ *Witters v. Sowles*, 32 Fed. 767, 35 Fed. 640; *Keyser v. Hitz*, 133 U. S. 138, 10 Sup. Ct. 290; *Robinson v. Tunentine*, 59 Fed. 554; note, 15 C. C. A. 132, 133; *In re Reciprocity Bank*, 22 N. Y. 9; *Sayles v. Bates*, 15 R. I. 342. 5 Atl. 497.

Death of Stockholder—Survival of Liability

If the liability imposed by a statute upon the corporation is contractual, the cause of action survives upon his death, but survives, and may be enforced by his representatives.¹⁸⁰ But if, on the other hand, the liability is within the rule, "Actio personalis moritur cum persona," it abates.¹⁸¹ The estate of a deceased stockholder is not liable for contracts contracted after his death, and while it owes no liability.

Forfeiture of Stock.

One whose stock is forfeited for nonpayment of dividends to creditors either for the unpaid balance of dividends or for the unpaid balance of dividends imposed by statutes imposing additional liability, when the forfeiture is to deprive the stockholder of his character as a shareholder, is true only when the forfeiture is in good faith and not fraudulent.¹⁸²

Holders of Unauthorized Stock.

Holders of certificates of unauthorized stock, issued by an unauthorized increase of stock, incur no liability to the creditors who did not rely on the validity of the stock. There is an estoppel on the part of the holders to deny the validity of the stock if there was no power at all to increase the stock of the corporation against creditors, for they are chargeable with notice of the power.¹⁸³ Where, however, the increase of stock was authorized by the corporation, so that it could have lawfully issued the stock, the corporation merely failed to take the preliminary steps to amend the charter, so that the creditors were not estopped to deny the validity of the stock to the holders.

¹⁸⁰ *Richmond v. Irons*, 121 U. S. 27, 7 Sup. Ct. 100, 31 N. Y. 399, 23 N. E. 803; *Grew v. Breed*, 10 Met. 503.

¹⁸¹ *Diversey v. Smith*, 103 Ill. 378, 9 Ill. App. 411.

¹⁸² *Bailey v. Hollister*, 26 N. Y. 112.

¹⁸³ *Mills v. Stewart*, 41 N. Y. 384. See ante, § 280, for the effect.

¹⁸⁴ *Sayles v. Brown*, 40 Fed. 8.

¹⁸⁵ *Scovill v. Thayer*, 105 U. S. 143.

¹⁸⁶ *Veeder v. Mudgett*, 95 N. Y. 295.

SAME—WHO MAY ENFORCE STATUTORY LIABILITY.

232. Unless otherwise provided, no one but a creditor can enforce the statutory liability of a stockholder. It cannot be enforced by the corporation, nor by its assignee for the benefit of creditors, nor by its assignee in bankruptcy or insolvency, nor a receiver.

233. A stockholder who is also a creditor is entitled to the benefit of the statute.

The statutory liability of stockholders for the debts of the corporation is created in favor of the creditors of the corporation, and not in any legal sense for the benefit of the corporation. It is not like the liability of stockholders for unpaid subscriptions. The liability is to the creditors, and not to the corporation. It follows that the liability can be enforced only by the creditors. It cannot be enforced by the corporation, nor by its assignee for the benefit of creditors, nor by its receiver or assignee in bankruptcy. Neither the corporation nor its assignee or receiver has any legal or equitable title, right, or interest therein.¹⁸⁷ Sometimes the right to enforce this liability is expressly given by statute to others than the creditors.¹⁸⁸

Stockholders Who are Creditors or Officers.

Under a statute making stockholders liable for the debts of the corporation to the extent of their shares, in addition to the amount that may be due on their shares, stockholders who are themselves creditors are entitled to come in equally with the other creditors.¹⁸⁹ But the statute is not intended to, and does not, include directors to whom the corporation is indebted for salaries.¹⁹⁰ When a stockholder who is liable severally and jointly with the other stockholders for the debts of the corporation is himself a creditor of the corporation, he

¹⁸⁷ *Dutcher v. Bank*, 12 Blatchf. 435, Fed. Cas. No. 4,203; *Bristol v. Sanford*, 12 Blatchf. 341, Fed. Cas. No. 1,898; *Jacobson v. Allen*, 12 Fed. 454; *Farnsworth v. Wood*, 91 N. Y. 308.

¹⁸⁸ See *Story v. Furman*, 25 N. Y. 214.

¹⁸⁹ *Briggs v. Penniman*, 8 Cow. (N. Y.) 387.

¹⁹⁰ *McDowall v. Sheehan*, 129 N. Y. 200, 29 N. E. 299.

§§ 234-236) RELATION BETWEEN CREDITORS AND

cannot generally maintain an action at law against a stockholder, or seize his property on execution, when he is a creditor; for that would enable him to collect not only all that such stockholder is ultimately liable for, but all that the entire body of stockholders, including himself, may have to pay, thus, as it was put by Judge Thomas, "collecting what he must pay with his left." His remedy is by contribution.¹⁹¹

SAME—REMEDIES OF CREDITORS AGAINST STOCKHOLDERS.

234. The liability of stockholders on account of their subscriptions may be enforced in an action at law or in equity, or by an assignee in bankruptcy or an assignee under a voluntary assignment for the benefit of creditors; but only creditors can enforce the statutory liability, unless otherwise provided.

235. To enforce the common-law liability of stockholders on their subscriptions, creditors

(a) Cannot maintain an action at law, but may do so by statute.

(b) But they may maintain a bill in equity.

(c) By the weight of authority, the statute giving a creditor the right to maintain a bill in equity to enforce the personal liability of stockholders, is in the nature of a creditors' bill, on behalf of the creditors who may come in.

(d) By the weight of authority, all the stockholders must be made parties, but the suit may be brought against a single stockholder, to compel him to contribute from the others.

¹⁹¹ *Thayer v. Tool Co.*, 4 Gray (Mass.) 75, 78. And see *15 Fed. 353*; *Balley v. Bancker*, 8 Hill (N. Y.) 188. In the Massachusetts case that a creditor, who is also a member of the corporation, may maintain a bill in equity to enforce the personal liability of stockholders, is in the nature of a creditors' bill, on behalf of the creditors who may come in. *Machine Co.*, 127 Mass. 592.

- (e) The corporation must be made a party, but its non-joinder may be waived by the stockholder.
- (f) Statutory remedies are given in some states, but they do not exclude the remedy in equity, unless by their express terms.

236. The remedy of creditors to enforce the statutory liability will depend upon the nature of the liability, unless the remedy is prescribed by the statute. Though there is confusion and conflict in the cases, by the weight of authority,

- (a) If the statute prescribes a remedy it is exclusive.
- (b) If the object of the statute is to provide a fund out of which all the creditors are to be paid pro rata, and to make the creditors contribute to it in proportion to their stock, the remedy is by general creditors' bill, or suit of that nature, and an action at law by a single creditor will not lie. Nor can the creditors severally maintain a bill in equity against the stockholders.
- (c) But if each stockholder is made severally liable directly to creditors, and his liability is fixed, and does not depend upon the liability of the others, any creditor who has observed conditions precedent ¹⁹² may sue a single stockholder at law.
- (d) In such a case each stockholder must be sued separately.
- (e) In such a case some courts hold that an action at law is the only remedy, while others allow an action at law, or a suit in equity, at the option of the creditor.

Common-Law Liability on Subscriptions, etc.—Action by Assignee for Creditors or in Bankruptcy.

Unpaid subscriptions, being a part of the assets of the corporation for the payment of its debts, pass to the assignee under a general as-

¹⁹² As to necessity for judgment and execution unsatisfied against the corporation, see post, p. 597.

signment for the benefit of creditors, and may be enforced by him for the creditors.¹⁹³ And they also pass to, and an action may be maintained by, an assignee in bankruptcy or receiver of the corporation.¹⁹⁴ In these cases the assignee or receiver stands in the place of the corporation, and is the only party to sue for unpaid subscriptions.¹⁹⁵ He may maintain an action at law. He is not, like a creditor, bound to sue in equity.

Same—Action at Law by Creditors.

Sometimes, by statute, creditors of a corporation are given a remedy by action at law or garnishment to subject unpaid subscriptions to stock to the satisfaction of their claims, when they have exhausted their remedies against the corporation.¹⁹⁶ But at common law a creditor cannot maintain an action at law against stockholders for unpaid subscriptions, for there is no privity of contract between them, and, furthermore, unpaid subscriptions cannot thus be appropriated by one creditor to the exclusion of the others. As was pointed out by Chief Justice Waite: "The liability of stockholders to creditors for unpaid subscriptions is through the corporation, not direct. * * * The stockholder is liable to the extent that the subscription represented by his stock requires him to contribute to the corporate funds, and, when sued for the money he owes, it must be in a way to put what he pays directly or indirectly into the treasury of the corporation for distribution according to law." He then adds that "no one creditor can assume that he alone is entitled to what any stockholder owes, and sue at law, so as to appropriate it exclusively to himself."¹⁹⁷

Same—General Creditors' Bill in Equity—Suit for Appointment of Receiver.

All the courts agree that a judgment creditor of a corporation, who has exhausted his remedy at law, may maintain a suit in equity on

¹⁹³ Germantown Pass. Ry. Co. v. Fitter, 60 Pa. St. 124; Citizens' & Miners' Sav. Bank & Trust Co. v. Gillespie, 115 Pa. St. 564, 9 Atl. 73; Chamberlain v. Bromberg, 83 Ala. 576, 3 South. 434.

¹⁹⁴ Scovill v. Thayer, 105 U. S. 143; Sawyer v. Hoag, 17 Wall. 610, 1 Cumming, Cas. Priv. Corp. 818; Dayton v. Borst, 31 N. Y. 435.

¹⁹⁵ Rankine v. Elliott, 16 N. Y. 377.

¹⁹⁶ See Fehr v. Gasch (Ill.) 44 N. E. 724.

¹⁹⁷ Patterson v. Lynde, 106 U. S. 520, 1 Sup. Ct. 432; Ladd v. Cartwright, 7 Or. 329; Brundage v. Mining Co., 12 Or. 322, 7 Pac. 314.

his own behalf, and on behalf of such other creditors of the corporation as may become parties with him, against the corporation and its delinquent stockholders, and have a decree that an account of the assets and debts of the corporation be taken, and that the stockholders pay in so much as may be due from them, respectively, to the corporation on account of their capital stock, or on account of property unlawfully distributed to them, as may be sufficient to pay the debts of the complainant and such other creditors as may join.¹⁹⁸ The bill must be a general creditors' bill, so as to allow other creditors to come in; for all the creditors are entitled to share in the assets of the corporation, and one cannot appropriate the whole, or more than his proportion.¹⁹⁹ A creditor, instead of maintaining such a suit may sue for the appointment of a receiver to collect and distribute the assets of an insolvent corporation, including unpaid subscriptions.²⁰⁰

Same—Parties.

By the great weight of authority, a creditor may, by a general creditors' bill, proceed against a single delinquent stockholder of an insolvent corporation, and compel him to pay the whole amount due from him to the corporation on account of his subscription, or on account of corporate property unlawfully received by him, if necessary in order to satisfy his debt, without making other stockholders parties, and without any account being taken of other indebtedness of the

¹⁹⁸ See *Burke v. Smith*, 16 Wall. 390; *Ogilvie v. Insurance Co.*, 22 How. 380, 1 Cumming, Cas. Priv. Corp. 814; *Briggs v. Penniman*, 8 Cow. (N. Y.) 387; *Hatch v. Dana*, 101 U. S. 205; *Holmes v. Sherwood*, 16 Fed. 725; *Bissit v. Navigation Co.*, 15 Fed. 353; *Spear v. Grant*, 16 Mass. 9; *Mann v. Pentz*, 3 N. Y. 415; *Hastings v. Drew*, 76 N. Y. 9; *Wetherbee v. Baker*, 35 N. J. Eq. 501; *Adler v. Manufacturing Co.*, 13 Wis. 63; *Barron v. Paine*, 83 Me. 312, 22 Atl. 218; *Henry v. Railroad Co.*, 17 Ohio, 187; *Umsted v. Buskirk*, 17 Ohio St. 113; *Payne v. Bullard*, 23 Miss. 88; *Brundage v. Mining Co.*, 12 Or. 322, 7 Pac. 314.

¹⁹⁹ See *Patterson v. Lynde*, 106 U. S. 520, 1 Sup. Ct. 432; *Wetherbee v. Baker*, 35 N. J. Eq. 501; *Cleveland Rolling-Mill Co. v. Texas & St. L. Ry. Co.*, 27 Fed. 250; *First Nat. Bank v. Peavey*, 75 Fed. 154.

²⁰⁰ *Rankine v. Elliott*, 16 N. Y. 377; *Mann v. Pentz*, 3 N. Y. 415; *Dayton v. Borst*, 31 N. Y. 435; *Brassey v. Railroad Co.*, 19 Fed. 663. See *Fosdick v. Schall*, 99 U. S. 235; *Platt v. Railroad Co.*, 65 Fed. 872.

corporation, the stockholder proceeded against being left to pursue his remedy against the other stockholders for contribution.²⁰¹

In Pennsylvania and in other states, it seems, the rule is different. It is there held that a bill filed by a creditor of an alleged insolvent corporation against one or several stockholders, to compel payment of their subscriptions, is a proceeding to enforce the equitable obligations of the stockholders, and that, inasmuch as only so much of the unpaid capital as is necessary for the payment of debts can be called in, and that can be done only when all the other assets are exhausted, an account must be taken of the amount of debts, assets, and unpaid capital, and a decree be made for an assessment of the amount due by each stockholder.²⁰² This does not apply where an assignee for the benefit of creditors sues to recover unpaid subscriptions, and the whole of them is required to pay the debts of the company.²⁰³

The corporation must be made a party to a suit by its creditor against delinquent stockholders, for otherwise it would not be bound by the judgment therein. But, if a stockholder sees fit to go to trial and judgment without objecting to the nonjoinder of the corporation, he cannot afterwards complain.²⁰⁴

Same—Necessity for Calls.

Where, by the charter or by-laws, or by the terms of the subscription itself, a call is necessary to render a subscriber liable on his subscription,²⁰⁵ an unpaid subscription cannot be enforced, either by an assignee for the benefit of creditors, or by a creditor, until a call has been duly made.²⁰⁶ But a court of equity will compel the directors to

²⁰¹ Hatch v. Dana, 101 U. S. 205; Ogilvie v. Insurance Co., 22 How. 380, 1 Cumming, Cas. Priv. Corp. 814; Marsh v. Burroughs, Fed. Cas. No. 9,112; Holmes v. Sherwood, 16 Fed. 725; Bartlett v. Drew, 57 N. Y. 587; Pierce v. Construction Co., 38 Wis. 253; Baines v. Babcock, 95 Cal. 581, 27 Pac. 675, 30 Pac. 776; Brundage v. Mining Co., 12 Or. 322, 7 Pac. 314.

²⁰² Lane's Appeal, 105 Pa. St. 49; Bell's Appeal, 115 Pa. St. 88, 8 Atl. 177; Wetherbee v. Baker, 35 N. J. Eq. 501.

²⁰³ Citizens' & Miners' Sav. Bank & Trust Co. v. Gillespie, 115 Pa. St. 564, 9 Atl. 73.

²⁰⁴ Potter v. Dear, 95 Cal. 578, 27 Pac. 676, 30 Pac. 777; Wetherbee v. Baker 35 N. J. Eq. 501.

²⁰⁵ Ante, p. 322, as to the necessity for calls.

²⁰⁶ Germantown Pass. Ry. Co. v. Fitler, 60 Pa. St. 124.

make the calls necessary to render subscribers liable,²⁰⁷ or it will, in effect, make the call itself, by a decree calling upon the subscribers to pay. Calls in such a case need not have been made by the company.²⁰⁸

Same—Statutory Remedies.

In some states statutory remedies are given creditors of a corporation, against delinquent stockholders, which do not exist at common law, nor in equity without the aid of the statute. Sometimes an action at law is allowed directly against the delinquent stockholder, or the process of garnishment is allowed. Sometimes a creditor who has recovered judgment against the corporation, on which execution has been returned unsatisfied, is allowed to issue execution directly against the stockholders. Unless the statutory remedy is expressly made exclusive, it does not prevent a creditor from pursuing his equitable remedy.²⁰⁹

Statutory Liability.

It is impossible to reconcile the decisions in the different states as to what is the proper remedy to enforce the statutory liability of stockholders for corporate debts.

As we have seen, the statutory liability of stockholders can only be enforced by the creditors. It cannot be enforced by an assignee in bankruptcy or insolvency, nor by an assignee under a voluntary assignment for the benefit of creditors.²¹⁰

Where the Statute Gives a Remedy.

It seems clear that where a liability is imposed by statute upon stockholders for the debts of the corporation, which did not exist at common law, nor in equity, independently of the statute, and the statute provides a remedy by which to enforce the liability, that remedy is exclusive, and must be strictly followed.²¹¹ Thus, it has been held

²⁰⁷ Germantown Pass. Ry. Co. v. Fidler, 60 Pa. St. 124.

²⁰⁸ Hatch v. Dana, 101 U. S. 205; Henry v. Railroad Co., 17 Ohio, 187; Washington Sav. Bank v. Butchers' & Drovers' Bank, 107 Mo. 133, 17 S. W. 644; Dalton & M. R. Co. v. McDaniel, 56 Ga. 191.

²⁰⁹ Potter v. Dear, 95 Cal. 578, 27 Pac. 676, 30 Pac. 777; Holmes v. Sherwood, 16 Fed. 725; Payne v. Bullard, 23 Miss. 88.

²¹⁰ Ante, p. 588.

²¹¹ Fourth Nat. Bank v. Francklyn, 120 U. S. 747, 7 Sup. Ct. 757; Morley v. Thayer, 3 Fed. 737; Lowry v. Inman, 46 N. Y. 120; Dauchy v. Brown, 24 Vt. 197; Knowlton v. Ackley, 8 Cush. (Mass.) 93; Cambridge Water-Works v. Som-

that, if the statute gives a remedy by action at law against a stockholder or stockholders, a bill in equity will not lie.²¹² So, where a charter only authorizes the taking of the individual property of stockholders on execution on a judgment against the corporation, and provides that the same process may be used and enforced by such stockholders against the property of the other stockholders, so as to compel a ratable contribution by all, no general individual liability is created for which a personal action will lie.²¹³

Same—Where No Remedy is Prescribed.

When the statute provides no remedy, there is more difficulty, and it is here that we meet with confusion and conflict in the decisions. Whether the remedy is at law or in equity, and whether suit must be brought on behalf of all the creditors, or may be brought by one creditor against a single stockholder, must depend upon the nature of the liability created. Special attention, therefore, must be given to the language of the particular statute. By the weight of authority, if the object of the statute is to provide a fund out of which all the creditors are to be paid, share and share alike, and to make the stockholders contribute to it in proportion to their stock, the remedy is by a general creditors' bill, or suit of that nature, in which an account may be taken of the debts and stock, and a pro rata distribution may be made among the several shareholders, and the fund thus obtained may be paid pro rata to all the creditors. And, under such a statute, an action at law by a single creditor against a single stockholder will not lie.²¹⁴ Nor can the creditors severally maintain a bill in equity against the stockholders.²¹⁵

But if, on the other hand, each stockholder is made severally liable

erville Dyeing & Bleaching Co., 4 Allen (Mass.) 239. This is true whether the proceedings are taken in the state creating the corporation or elsewhere, and whether in the state or federal courts. *Fourth Nat. Bank v. Francklyn, supra.*

²¹² *Morley v. Thayer, supra.*

²¹³ *Lowry v. Inman, supra.*

²¹⁴ *Terry v. Little, 101 U. S. 216.* In this case the statute declared that the stockholders should be "liable and held bound * * * for any sum not exceeding twice the amount of their shares," and it was held that an action at law could not be maintained by a single creditor against two of a large number of stock-

²¹⁵ *Crease v. Babcock, 10 Metc. (Mass.) 525.*

directly to creditors, and his liability is fixed, and does not depend upon the liability of the other stockholders, so that there is no necessity to bring in the other stockholders or creditors, any creditor who has recovered judgment against the corporation, and had execution returned unsatisfied, where this is necessary, or without this where it is unnecessary, may maintain an action at law against a single stockholder.²¹⁶ Where the liability of the stockholders is several, and an action at law is brought, each must be sued separately.²¹⁷

Where the statute thus imposes an unconditional, original, and immediate liability on the part of a stockholder to creditors, it is held by the supreme court of the United States, and other courts, that the remedy must be sought at law, and not in equity, unless there are some peculiar circumstances giving rise to a claim for equitable relief, but that a suit in equity will lie if there are such circumstances. In other words, "the jurisdiction may be regarded as concurrent, both at law and in equity, according to the nature of the relief made neces-

holders. See, also, *Pollard v. Bailey*, 20 Wall. 520; *Terry v. Tubman*, 92 U. S. 156; *Crease v. Babcock*, 10 Metc. (Mass.) 525, 531; *Harris v. First Parish*, 23 Pick. (Mass.) 112; *Coleman v. White*, 14 Wis. 700; *Oleveland v. Burnham*, 55 Wis. 598, 18 N. W. 677; *Jones v. Jarman*, 34 Ark. 340; *Johnson v. Fischer*, 30 Minn. 173, 14 N. W. 799; *Queenan v. Palmer*, 117 Ill. 619, 7 N. E. 613. See *Barrick v. Gifford*, 47 Ohio St. 180, 24 N. E. 259. The decisions in New York are to the contrary, and allow an action at law. See cases cited in notes 216, 219, *infra*.

²¹⁶ *Flash v. Conn*, 109 U. S. 371, 3 Sup. Ct. 263. In this case the statute provided that the stockholders should be "severally individually liable to the creditors of the company * * * to an amount equal to the amount of stock held by them, respectively," for all debts and contracts made by the company, until the whole amount of the capital stock should be paid in, and a certificate thereof recorded. It was held that the liability was fixed, and that any creditor who had recovered judgment against the company, and sued out execution thereon, which was returned unsatisfied, might sue any stockholder in an action at law, there being no necessity to resort to a court of equity to ascertain the extent of the liability. And see *Hall v. Klinck*, 25 S. C. 348, 60 Am. Rep. 505; *Fuller v. Ledden*, 87 Ill. 310; *Buchanan v. Meisser*, 105 Ill. 638; *Thompson v. Meisser*, 108 Ill. 359; *Schalucky v. Field*, 124 Ill. 617, 16 N. E. 904; *Bank of Poughkeepsie v. Ibbotson*, 24 Wend. (N. Y.) 473; *Garrison v. Howe*, 17 N. Y. 458; *Weeks v. Love*, 50 N. Y. 508.

²¹⁷ *Abbey v. Dry Goods Co.*, 44 Kan. 415, 24 Pac. 426; *Perry v. Turner*, 55 Mo. 418.

§ 237.) RELATION BETWEEN CREDITORS AND

sary by the circumstances upon which the
York and some other jurisdictions, however
at law will lie, it is held that the creditor may
equity.²¹⁹

A creditors' bill in equity, or suit in the
will lie where it is sought to enforce, not only
of the stockholders, but also to compel pay-
ments.²²⁰

**SAME—NECESSITY FOR JUDGMENT
TION.**

**237. Ordinarily recovery of a judgment
against a corporation, and return of ex-
cess of assets, are conditions precedent to a suit
against the stockholders. There is, however,
in some of the decisions.**

It is well settled that a creditor cannot
sue against stockholders to compel payment of
subscriptions, or repayment of funds paid out,
until he has exhausted his legal remedy against the corporation.
rule, therefore, to maintain such a suit he
must first sue against the corporation, and a return of ex-
cess of assets must be obtained.²²¹ Such a return is sufficient proof that
the legal remedy against the corporation has been exhausted.²²²

²¹⁸ *Manufacturing Co. v. Bradley*, 105 U. S. 177,
185; *Tunesma v. Schuttler*, 114 Ill. 156, 28 N. E. 6.

²¹⁹ *Bank of Poughkeepsie v. Ibbotson*, 24 Wend.
Howe, 17 N. Y. 458; *Mathez v. Neidig*, 72 N. Y. 1
568; *Pfohl v. Simpson*, 74 N. Y. 137; *Briggs v. Peck*.

²²⁰ *Barrick v. Gifford*, 47 Ohio St. 180, 24 N. E.

²²¹ *National Tube Works Co. v. Ballou*, 146 U. S. 1
Land & Cattle Co. v. Frank, 148 U. S. 603, 13 Sup.
Co., 140 Mass. 494, 5 N. E. 292; *Sturges v. Vanderbilt*.

²²² *Baines v. Babcock*, 95 Cal. 581, 27 Pac. 674,
held that he should, if possible, obtain a judgment
in the jurisdiction in which he proposes to sue in equity.
This is the rule in the federal courts. Therefore
v. Ballou, supra, it was held that a creditors' bill

It is expressly provided in most statutes that the personal statutory liability of stockholders for debts of the corporation shall arise only after a recovery by the creditor of a judgment against the corporation, and an exhaustion of his legal remedy by execution, and a return of no property found, unless the corporation has been dissolved, or put in process of winding up, so that no judgment can be obtained against it. Under such a statute, unless the case comes within the exception, recovery of judgment against the corporation, and a return of execution unsatisfied, is a condition precedent to any liability on the part of the stockholders.²²³

Some courts hold that, where there is no such provision, the remedy inures to all creditors, whether they have recovered judgments against the corporation or not, and that, upon default of the corporation, any creditor may sue any stockholder.²²⁴ Other courts hold that, even in the absence of such a provision, the creditor must exhaust his remedy against the corporation before proceeding against stockholders, by recovery of judgment and issue of execution, for the liability of the stockholders is not to be regarded as a primary resource of the creditors.²²⁵ It has been held, however, that where the corporation has become insolvent and made an assignment for the benefit of its creditors, or has been adjudicated a bankrupt, etc., the right of the creditors then accrues to commence suit against the stockholders, without any prior proceedings against the company.²²⁶

covered in Connecticut against a corporation of that state, could not be maintained in a United States circuit court in New York, against a citizen of that state, to enforce his liability on an unpaid subscription to the stock of the corporation, where no judgment had been obtained or execution issued against the corporation within the latter state, and no allegations were made showing that it was impossible to obtain such a judgment.

²²³ *Morley v. Thayer*, 3 Fed. 737; *Rocky Mountain Nat. Bank v. Bliss*, 89 N. Y. 338. And see *Cambridge Waterworks v. Somerville Dyeing & Bleaching Co.*, 4 Allen (Mass.) 239.

²²⁴ *McDonnell v. Insurance Co.*, 85 Ala. 401, 5 South. 120; *Schalucky v. Field*, 124 Ill. 617, 16 N. E. 904.

²²⁵ *Barrick v. Gifford*, 47 Ohio St. 180, 24 N. E. 259; *Wright v. McCormack*, 17 Ohio St. 86. And see *Rocky Mountain Nat. Bank v. Bliss*, 89 N. Y. 338; *Bronson v. Schneider*, 49 Ohio St. 438, 33 N. E. 233; *Younglove v. Lime Co.*, 49 Ohio St. 663, 33 N. E. 234.

²²⁶ *Barrick v. Gifford*, 47 Ohio St. 180, 24 N. E. 259; *Shellington v. Howland*, 53 N. Y. 371; *Flash v. Conn*, 109 U. S. 371, 3 Sup. Ct. 263; *Bronson v. Schnel-*

SAME—EFFECT OF JUDGMENT AGAINST CORPORATION.

238. There is a difference of opinion as to the effect of a judgment against the corporation as evidence of its indebtedness as against a stockholder. The decisions are thus:

- (a) Where it is sought to enforce a statutory liability, it is *prima facie* evidence of indebtedness, except where the liability is penal.
- (b) Some courts hold it conclusive, in the absence of fraud or want of jurisdiction.
- (c) Where it is sought to enforce the common-law liability on account of stock, it is conclusive, in the absence of fraud or want of jurisdiction.

A judgment recovered against a corporation is generally *prima facie*, but not conclusive, evidence of indebtedness against the company, in an action against a stockholder to enforce his individual statutory liability.²²⁷ Some courts have held the judgment against the corporation to be conclusive evidence of the debt in the absence of fraud or want of jurisdiction;²²⁸ but, by the weight of authority, it is only *prima facie* evidence, the stockholders not having been parties to the action in which it was recovered.²²⁹ It is not even *prima facie* evidence where the liability which it is sought to impose upon the stockholder is original and penal in its character.²³⁰

der, 49 Ohio St. 438, 33 N. E. 233; *Younglove v. Lime Co.*, 49 Ohio St. 663, 33 N. E. 234. Contra, *Morley v. Thayer*, 3 Fed. 737.

²²⁷ *Belmont v. Coleman*, 21 N. Y. 96; *Moss v. McCullough*, 5 Hill (N. Y.) 131; *Terry v. Tubman*, 92 U. S. 156; *Hastings v. Drew*, 76 N. Y. 9; *Stephens v. Fox*, 83 N. Y. 313.

²²⁸ *Slee v. Bloom*, 20 Johns. (N. Y.) 669; *Miller v. White*, 59 Barb. (N. Y.) 434 (reversed in 50 N. Y. 137); *Farnum v. Ballard Vale Machine Shop*, 12 Cush. (Mass.) 507. So under the Massachusetts statute by which a summons in the action against the corporation was required to be served on stockholders, and they were permitted to defend in such action, etc. *Holyoke Bank v. Goodman Paper Manuf'g Co.*, 9 Cush. (Mass.) 576.

²²⁹ Cases in note 227, *supra*.

²³⁰ *Miller v. White*, 50 N. Y. 137; *McMahon v. Macy*, 51 N. Y. 153. See explanation of these cases in *Hastings v. Drew*, 76 N. Y. 9, and *Stephens v. Fox*, 83 N. Y. 313.

A judgment regularly obtained against a corporation is conclusive against a stockholder, in the absence of fraud, where the suit against him is to compel payment of his subscription to the stock of the corporation, or to compel him to refund property of the corporation unlawfully received by him.²³¹ In such a case, however, it may be attacked for collusion and fraud.²³²

SAME—STATUTE OF LIMITATIONS.

239. The statute of limitations runs against an action by creditors to enforce against stockholders liability on account of their stock from the time an action can be maintained, which is generally when a valid call is made by the corporation or by a court of equity in a suit by creditors. The statute runs against an action to enforce the statutory liability of stockholders from the time when a cause of action accrues, which is generally from the return of execution against the corporation. The rule will vary, however, according to the terms of the statute.

Liability on Subscription.

Some of the courts have held that the liability of stockholders to pay their subscriptions is a direct trust, and that the statute of limitations, therefore, does not run against it, at least until a call is made by the corporation or other proper authority. "If the corporation," it has been said, "does not compel payment of the stock, the subscribers must be deemed to hold it for the corporation, subject to its call. It is a continuing, subsisting trust and confidence, to which the statute of limitations has no application."²³³ The true relation, however, between a stockholder and the corporation, with respect to his unpaid subscription, is that of debtor and creditor. There is really no trust at all, either as to the corporation or its creditors.²³⁴ There is simply

²³¹ *Barron v. Paine*, 83 Me. 312, 22 Atl. 218; *Bissit v. Navigation Co.*, 15 Fed. 853; *Tatum v. Rosenthal*, 95 Cal. 129, 30 Pac. 136.

²³² *Bissit v. Navigation Co.*, 15 Fed. 353.

²³³ *Payne v. Bullard*, 23 Miss. 88. And see *Hightower v. Thornton*, 8 Ga. 486; *Mack's Appeal* (Pa. Sup.) 7 Atl. 481.

²³⁴ Ante, p. 539 et seq.

a debt, a contract; and, in reason, the statute runs when a cause of action thereon accrues payable on demand, or on call, the statute is duly made, and not before then.²³⁶ If a corporation ceases to do business, no call by the stockholders renders stockholders liable, but there must be a demand or call by a receiver, assignee, or debtor. The statute does not begin to run until then.²³⁷ If a creditor who has recovered a judgment against a stockholder, the cause of action accrues against the corporation on an execution on a judgment against the corporation is unsatisfied, and the statute runs from that time. Courts have held that the statute runs against an action to subject the balance due by him on his stock to a judgment obtained against the corporation. The cause of action accrued against the corporation.

Statutory Liability.

Sometimes the statute creating the liability fixes the time within which an action must be brought to enforce the same. Where this is not the case the time is fixed on the nature of the liability. If it is contract, the statute relating to actions on contract governs.

²³⁵ See *Lake Ontario, A. & N. Y. R. Co. v. Masc*

²³⁶ *Great Western Tel. Co. v. Gray*, 122 Ill. 630; *Taylor*, 120 N. Y. 244, 24 N. E. 288; and cases in the same line.

²³⁷ *Glenn v. Marbury*, 145 U. S. 499, 12 Sup. Ct. 143; *Glenn v. Semple*, 80 Ala. 159; *Lehm v. Ala.* 618, 6 South. 44; *Glenn v. Williams*, 60 Md. 319, 9 Sup. Ct. 739; *Washington Sav. Bank*, 107 Mo. 183, 17 S. W. 644; *Great Western v. Vanderwerken v. Glenn*, 85 Va. 9, 6 S. E. 806; *8 S. E. 636*. In Pennsylvania it is held that when a corporation is solvent, and makes an assignment, the statute begins to run from the date of assignment. *Franklin Sav. Bank v. Bridges* (Pa.).

²³⁸ *Washington Sav. Bank v. Butchers' & Drovers' Bank*, 107 Mo. 183, 17 S. W. 644.

²³⁹ *First Nat. Bank v. Greene*, 64 Iowa, 445, 17

is penal, the case is governed by the clause relating to actions upon a statute for a penalty or forfeiture.²⁴⁰

The statute of limitations begins to run as soon as creditors acquire a right to sue the stockholders. Where the statute requires recovery of judgment against the corporation, and issue of execution, and return of no property found, it does not begin to run until then; that is, until the return of the execution.²⁴¹ If a right of action accrues on the insolvency or dissolution of the corporation, or an assignment for creditors, and no judgment against the corporation is necessary, the statute runs from that time.²⁴² If the statute makes the stockholders liable as principal debtors, the liability accrues against the corporation and the stockholders at the same time, and suspension of the remedy against the corporation, as by a renewal of the debt, does not suspend the remedy against, or affect the liability of, the stockholders.²⁴³ A suit commenced by one creditor on behalf of himself and all others—that is, a general creditors' bill—is in the nature of a demand for all, and stops the running of the statute as against all creditors who may come in and assert their claims.²⁴⁴

SAME—SET-OFF BY STOCKHOLDERS.

240. A stockholder who is also a creditor of the corporation cannot set off his claim, either against his liability on his subscription, or his liability for corporate funds unlawfully received by him, or against

²⁴⁰ *Wyles v. Suydam*, 64 N. Y. 173; *Merchants' Bank of New Haven v. Bliss*, 35 N. Y. 412; *Corning v. McCullough*, 1 N. Y. 47.

²⁴¹ *Taylor v. Bowker*, 111 U. S. 110, 4 Sup. Ct. 397; *Handy v. Draper*, 89 N. Y. 334; *Younglove v. Lime Co.*, 49 Ohio St. 663, 33 N. E. 234.

²⁴² *McDonnell v. Insurance Co.*, 85 Ala. 401, 5 South. 120; *Barrick v. Gifford*, 47 Ohio St. 180, 24 N. E. 259; *Bronson v. Schneider*, 49 Ohio St. 438, 33 N. E. 233; *Younglove v. Lime Co.*, 49 Ohio St. 663, 33 N. E. 234; *Terry v. Tubman*, 92 U. S. 156.

²⁴³ *Hyman v. Coleman*, 82 Cal. 650, 23 Pac. 62; *Parrott v. Colby*, 6 Hun (N. Y.) 57, 71 N. Y. 597; *Jagger Iron Co. v. Walker*, 76 N. Y. 521; *Schalucky v. Field*, 124 Ill. 617, 16 N. E. 904; *Coleman v. White*, 14 Wis. 700.

²⁴⁴ *Barrick v. Gifford*, 47 Ohio St. 180, 24 N. E. 259; *Richmond v. Irons*, 121 U. S. 27, 7 Sup. Ct. 788.

his statutory liability, if it
him contribute a proportion
ment of all creditors pro
where an action is brought
his sole benefit.

Where a stockholder of an insolvent corporation, is indebted to the corporation on account of property of the corporation unlawfully paid to him, or on account of undivided dividends, or on any other cause, the stockholder is to pay what he owes, and then come in with other creditors in all the assets of the corporation. He cannot sue upon his indebtedness by or for the corporation, but he may set off the debt due him from the corporation. He cannot be permitted to appropriate this asset to himself, but of his own claim to the exclusion of the claims of other creditors. If an action is brought by a single creditor against the corporation, he may set off a debt due him from the corporation, and he is not compelled to pay his indebtedness to the corporation until an action against all the stockholders is brought. If an action comes in with other creditors for the assets.²⁴⁰

The same rule applies where suit is brought by the corporation.

²⁴⁰ *Sawyer v. Hoag*, 17 Wall. 610; *Handley v. City of New York*, 100 N. Y. 530, 1 Cumming, Cas. Priv. Corp. 855; *Osborne v. Nelson*, 21 N. Y. 158; *Shickle v. Watts*, 100 N. Y. 158; *Carbon Co. v. Mills*, 78 Iowa, 460, 43 N. W. 28; *Wells v. Wells*, 79 Iowa, 653, 44 N. W. 797; *Hillier v. Williams*, 38 N. J. Eq. 57; *Thebus v. Thebus*, 84 Me. 72, 24 supra, the defendants, members of a mutual insurance company, were liable for a loss upon an insured vessel, which loss was recovered by the company. In proceedings to dissolve the company as insolvent, the receiver of the company to recover on the policies issued to them, it was held that the company's indebtedness for the loss. *Hillier v. Williams*, 38 N. J. Eq. 57. In most of the other cases cited above, the stockholders were liable for the loss, or to recover dividends unlawfully paid.

²⁴⁰ *Mathez v. Neidig*, 72 N. Y. 100.

enforce their statutory liability. If it is sought to compel them each to contribute a proportionate sum to a fund for the payment of all creditors pro rata, a set-off cannot be allowed.²⁴⁷ It is otherwise, however, where an action is brought by a single creditor, as may be done under some statutes, to enforce a several and original liability, to the amount of his stock, for the sole benefit of the creditor suing.²⁴⁸

SAME—CONTRIBUTION AMONG STOCKHOLDERS.

241. A stockholder is entitled to contribution from the other stockholders where he has paid more than his share of corporate debts, either.

(a) On account of a liability on his subscription, the other stockholders being also liable on their subscriptions,

²⁴⁷ *U. S. Trust Co. v. U. S. Fire Ins. Co. (In re Empire City Bank)*, 18 N. Y. 199.

²⁴⁸ *U. S. Trust Co. v. U. S. Fire Ins. Co. (In re Empire City Bank)*, 18 N. Y. 199, 227; *Garrison v. Howe*, 17 N. Y. 458; *Mathez v. Neidig*, 72 N. Y. 100; *Agate v. Sands*, 73 N. Y. 620; *Wheeler v. Millar*, 90 N. Y. 353. To entitle him to a set-off, he must be really a creditor of the corporation. He cannot set off a debt due him from the corporation if he owes the company, on his subscription, more than the amount of his claim against it. *Wheeler v. Millar*, *supra*. But where a stockholder had purchased up judgments against the corporation, while he was a director, and after he knew the company was insolvent, it was held that the judgments could avail him as a defense or set-off only to the amount actually paid for them. *Bulkley v. Whitcomb*, 121 N. Y. 107, 24 N. E. 13. And see *Abbey v. Long*, 44 Kan. 688, 24 Pac. 1111, where it was held that a stockholder, though not a director, cannot buy up claims against the corporation, and then set them off against his liability at their face value. And see *Thompson v. Meisser*, 108 Ill. 359; *Manville v. Karst*, 16 Fed. 175; *Kunkelman v. Rentschler*, 15 Ill. App. 271; *Gauch v. Harrison*, 12 Ill. App. 459; *Smith v. Mosby*, 9 Heisk. (Tenn.) 501; *Balch v. Wilson*, 25 Minn. 299. In *Manville v. Karst*, 16 Fed. 173, the defendant, a stockholder in an insolvent bank, became liable to creditors of the bank in the sum of \$1,200, under a double liability law, and was sued for that amount by a creditor. Before judgment could be had, he agreed with a friend that, if the latter would buy up claims against the bank to the amount of his liability, he would confess judgment in his favor, and the friend bought up claims at a large discount, from a stockholder in the bank, and the defendant confessed judgment in his favor for the full amount of the claims, and paid the same. It was held that the judgment and satisfaction could not avail him as a defense.

(b) Or on account of his statutory liability, where it is contractual, all the stockholders being jointly and severally liable.

(c) But not where the payment was on account of a penal statutory liability.

If the liability imposed by the statute for the debts of the company is penal, and not contractual, stockholders against whom creditors have enforced the liability cannot maintain a suit against other stockholders for contribution.²⁴⁹ It is otherwise, however, if the statute imposes a contractual liability upon the stockholders jointly and severally, and one of them is compelled to pay more than his share. In such a case he may file a bill in equity to enforce contribution from the other stockholders who were also liable.²⁵⁰ So, where stockholders are liable on their subscriptions, and one of them is compelled to pay the amount due from him to satisfy a corporate debt, he may sue for contribution.²⁵¹ Ordinarily contribution may be enforced by a suit in equity, but, if the statute prescribes a remedy, it must be followed.²⁵² A suit for contribution may be maintained against nonresident stockholders.²⁵³ Liability to contribute survives the death of a stockholder.²⁵⁴

RELATION BETWEEN CREDITORS AND OFFICERS.

242. There is no privity between the creditors of a corporation and its officers. And, strictly speaking, there is no trust relation.

243. The creditors of a corporation cannot maintain an action at law against its officers for fraud, negli-

²⁴⁹ Sayles v. Brown, 40 Fed. 8.

²⁵⁰ 1 Cook, Stock, Stockh. & Corp. Law, § 211; Redington v. Cornwell, 90 Cal. 49, 27 Pac. 40; Wincock v. Turpin, 96 Ill. 135; Allen v. Fairbanks, 40 Fed. 188, 45 Fed. 445; Koons v. Martin, 66 Hun, 554, 21 N. Y. Supp. 657. And see Wolters v. Henningsan (Cal.) 46 Pac. 277.

²⁵¹ Wincock v. Turpin, 96 Ill. 135; 1 Cook, Stock, Stockh. & Corp. Law, § 227.

²⁵² O'Reilly v. Bard, 105 Pa. St. 569.

²⁵³ Allen v. Fairbanks, 45 Fed. 445.

²⁵⁴ Allen v. Fairbanks, 40 Fed. 188.

gence, or other breach of duty to the corporation. But if the officers are liable to the corporation for fraud, negligence, or other wrongs, the liability constitutes an equitable asset of the corporation, and may be reached by its judgment creditors in equity.

The creditors of an insolvent corporation, according to all of the authorities, may, in order to procure satisfaction of their claims, enforce the liability of directors and other officers of the corporation for losses resulting from their mismanagement of the corporate affairs. Most of the courts have based the right of action in such cases upon the ground that the assets of a corporation are a trust fund for the benefit of creditors, and that the officers are trustees for their benefit.²⁵⁵ The trust-fund doctrine, however, has been virtually exploded, as we have seen, by late decisions of courts of the highest authority, and it is perhaps safe to say that no court would now hold directly that any trust relation exists between the officers and the creditors of a corporation.²⁵⁶ The true basis of the right of creditors to proceed against the officers of a corporation is in their right to reach equitable assets of the corporation and apply them to the satisfaction of their claims. The officers of a corporation, as we have seen, are liable to the corporation for losses caused by their fraud, gross negligence, or willful breach of duty, and this liability may be enforced by or for the benefit of creditors when the corporation becomes insolvent. It is the enforcement of their claims by creditors against equitable assets of the corporation.²⁵⁷

Whatever may be the grounds upon which the right of action is based by the different courts, it is well settled that where the officers of a corporation willfully misappropriate or misapply its assets, and the corporation becomes insolvent, the creditors who have recovered judgments against the corporation may hold them liable to the extent of the misappropriation.²⁵⁸ So if the officers of an insolvent

²⁵⁵ 1 Mor. Priv. Corp. § 568.

²⁵⁶ Ante, p. 539 et seq.

²⁵⁷ See 2 Mor. Priv. Corp. §§ 795, 796.

²⁵⁸ Gratz v. Redd, 4 B. Mon. (Ky.) 178, 195; Ellis v. Ward, 137 Ill. 509, 25

corporation have been grossly negligent in the performance of their duties, and the assets of the company have been thus allowed to be wasted, they may be held liable to creditors to the extent of the loss.²⁵⁹ Thus, if the assets of a bank are wasted through the mismanagement or gross negligence of the directors, the depositors may hold them liable.²⁶⁰

It is well settled, however, that the officers of a corporation, if they act in good faith within the limits of the powers conferred upon the corporation by its charter, and within their authority, and use a proper degree of prudence and diligence, are not responsible either to the corporation or to its creditors for losses resulting from mere mistakes or errors of judgment.²⁶¹ Thus, they are not liable for declaring or paying a dividend which diminishes the capital, in violation of a statute or the common law, where they are not guilty of bad faith or negligence.²⁶² Nor are they liable for losses from accident, theft, etc., where they have not been negligent.²⁶³ The directors of a corporation cannot be held liable to creditors of the corporation for the acts or omissions of other agents, unless they have been guilty of neglect in supervising or appointing them.²⁶⁴ What constitutes such negligence as will render officers of a corporation liable has been considered on a former page.²⁶⁵

A creditor of a corporation cannot sue its officers at law for fraud,

N. H. 531; *Wilkinson v. Bauerle*, 41 N. J. Eq. 635, 7 Atl. 514; *Moses v. Bank*, 1 Lea (Tenn.) 398; *Bank of St. Mary's v. St. John*, 25 Ala. 566; ante, p. 514 et seq.

²⁵⁹ *Hun v. Cary*, 82 N. Y. 65, 37 Am. Rep. 546; *Brinckerhoff v. Bostwick*, 88 N. Y. 52; *Marshall v. Bank*, 85 Va. 676, 8 S. E. 586; *Delano v. Case*, 17 Bradw. (Ill.) 531, 121 Ill. 247, 12 N. E. 676; *United Society of Shakers v. Underwood*, 9 Bush (Ky.) 609; *Gratz v. Redd*, 4 B. Mon. (Ky.) 178, 196; ante, p. 516.

²⁶⁰ See cases cited in the preceding note.

²⁶¹ *Spering's Appeal*, 71 Pa. St. 11, 10 Am. Rep. 684, 1 Cumming, Cas. Priv. Corp. 799; *Watt's Appeal*, 78 Pa. St. 370; *Williams v. McDonald*, 37 N. J. Eq. 409; ante, p. 515.

²⁶² *Excelsior Petroleum Co. v. Lacey*, 63 N. Y. 422; *Van Dyck v. McQuade*, 86 N. Y. 38; *Lexington & O. R. Co. v. Bridges*, 7 B. Mon. (Ky.) 556; ante, p. 515.

²⁶³ *Mowbray v. Antrim*, 123 Ind. 24, 23 N. E. 858.

²⁶⁴ *Briggs v. Spaulding*, 141 U. S. 132, 11 Sup. Ct. 924, 2 Cumming, Cas. Priv. Corp. 186, Shep. Cas. Corp. 200. And see *Savings Bank of Louisville's Assignee v. Caperton*, 87 Ky. 306, 8 S. W. 885.

²⁶⁵ Ante, p. 516.

negligence, or mismanagement in conducting the affairs of the corporation.²⁶⁶ The remedy is in equity, by creditors' bill.²⁶⁷ All the guilty officers need not be joined as parties, for their liability is several, but the corporation must be made a party.²⁶⁸

SAME—PREFERENCES TO OFFICERS WHO ARE CREDITORS.

244. When a corporation becomes insolvent and ceases to do business, the directors or other officers in charge of its assets cannot, by mortgage or otherwise, secure to themselves any preference or advantage over other creditors.

So long as a corporation is doing business, there is no privity whatever between the directors or other officers and its creditors. It has often been said that, when a corporation becomes insolvent and ceases to do business, a quasi trust relation arises between the officers and its creditors; that they hold the property of the corporation as a trust fund for the equal benefit of all the creditors; and that, if they are themselves creditors while the corporation is under their management, they cannot, by mortgage or otherwise, secure to themselves any preference or advantage over other creditors.²⁶⁹ It is undoubtedly the law in this country that officers of a corporation cannot prefer themselves over other creditors, under such circumstances, but it is not true that there is any real trust relation between them and the creditors; and to say that there is, and base the invalidity of the transaction on that ground, will tend to confuse. As a matter of fact, such a transaction is invalid as against the other creditors, because it is fraudulent as to them, and it is not necessary to look for any other reason.²⁷⁰ In England it has been expressly held that the directors of an insolvent corporation are not trustees for cred-

²⁶⁶ *Zinn v. Mendel*, 9 W. Va. 580; *Smith v. Poor*, 40 Me. 415; *Branch v. Roberts*, 50 Barb. (N. Y.) 435; *Fusz v. Spaunborst*, 67 Mo. 256.

²⁶⁷ *Schley v. Dixon*, 24 Ga. 273.

²⁶⁸ *Cunningham v. Pell*, 5 Paige (N. Y.) 607.

²⁶⁹ *Beach v. Miller*, 130 Ill. 162, 22 N. E. 464; *Wilkinson v. Bauerle*, 41 N. J. Eq. 635, 7 Atl. 514; *Olney v. Land Co.*, 16 R. I. 597, 18 Atl. 181; *Haywood v. Lumber Co.*, 64 Wis. 639, 26 N. W. 184; and cases hereafter cited.

²⁷⁰ That such preferences are void as against creditors is well settled, what-

itors; and it has further been held, contrary to the rule in this country, that in paying corporate debts, before proceedings to wind up the company have been instituted, they may prefer debts upon which they are themselves liable as guarantors.²⁷¹

SAME—STATUTORY LIABILITY OF OFFICERS.

245. In most states it is provided by statute that the directors or other officers of a corporation shall be liable for its debts, where they are guilty of certain official neglect or misconduct. These statutes, being penal, are strictly construed.

In most of the states, statutes have been enacted making the directors or other officers of a corporation liable for its debts where they are guilty of certain official neglect or misconduct, as of failure to make a report of the condition of the corporation required by law;²⁷² making false reports;²⁷³ allowing the debts of the corpo-

ever may be the ground of invalidity. See *Beach v. Miller*, 130 Ill. 162, 22 N. E. 464; *Roseboom v. Whittaker*, 132 Ill. 81, 23 N. E. 339; *Sicardi v. Oil Co.*, 149 Pa. St. 148, 24 Atl. 163; *Wilkinson v. Bauerle*, 41 N. J. Eq. 635, 7 Atl. 514; *Olney v. Land Co.*, 16 R. I. 597, 18 Atl. 181; *Adams v. Milling Co.*, 35 Fed. 433; *Corey v. Wadsworth*, 99 Ala. 68, 11 South. 350; *Gibson v. Furniture Co.*, 96 Ala. 357, 11 South. 365; *Hays v. Bank*, 51 Kan. 535, 33 Pac. 318; *Ingwersen v. Edgecombe*, 42 Neb. 740, 60 N. W. 1032. Thus, where a majority of the directors of a corporation, knowing it to be insolvent, vote for the execution to them of the corporation's judgment note, which is executed by one of their number as treasurer, and a judgment is immediately entered, the judgment is fraudulent and void as to other creditors, though the note was given in payment of a bona fide debt. *Roseboom v. Whittaker*, *supra*. This rule has been extended to include preferences given by officers to their relatives. *Adams v. Milling Co.*, *supra*. And it has been applied to conveyances by officers in payment of a debt on which they were liable as guarantors or sureties. *Goodyear Rubber Co. v. George D. Scott Co.*, 96 Ala. 439, 11 South. 370; *Richards v. Insurance Co.*, 43 N. H. 263.

²⁷¹ *Poole, Jackson & Whyte's Case* (In re Wincham Ship-Building, Boiler & Salt Co.), 9 Ch. Div. 322.

²⁷² *Bruce v. Platt*, 80 N. Y. 379; *Halsey v. McLean*, 12 Allen (Mass.) 438; *Gaus v. Switzer*, 9 Mont. 408, 24 Pac. 18. That the New York statute does not

²⁷³ As to the liability under such a provision, see *Pier v. Hanmore*, 86 N. Y. 95; *Matthews v. Patterson*, 16 Colo. 215, 26 Pac. 812.

ration to exceed the capital or a certain proportion of the capital;²⁷⁴ paying a dividend which diminishes the amount of the capital stock;²⁷⁵ failure to publish the articles of association;²⁷⁶ violating any of the provisions of the act under which the corporation is formed, whereby it shall become insolvent, etc.²⁷⁷ These statutes are highly penal, and are to be strictly construed. The liability cannot be extended beyond the strict terms of the statute, and a clear case must be established to render an officer liable.²⁷⁸

One of the directors or trustees, who is also a creditor of the corporation, cannot maintain an action under the statutes against his co-trustees or co-directors for breach of duty, and his assignee stands in the same position. To allow such an action would enable him to profit by his own wrong or negligence.²⁷⁹ But the liability may be enforced by a creditor who is a stockholder.²⁸⁰

Where an action is brought against a director under a statute making directors liable for the debts of the company if they fail to file a report, the plaintiff must establish the fact that he is a creditor of the company; and, by the weight of authority, proof of the recov-

require a report after the corporation has ceased to own property or do business, and has been practically dissolved, see *Bruce v. Platt*, 80 N. Y. 379, and cases there cited. See, also, *Kirkland v. Kille*, 99 N. Y. 395, 2 N. E. 86. But the mere fact that the company has ceased to do business, and is winding up its affairs, is no excuse for failure to file a report. *Sanborn v. Lefferts*, 58 N. Y. 179. And see *Gaus v. Switzer*, 9 Mont. 408, 24 Pac. 18. As to sufficiency of report, see *Bonnell v. Griswold*, 80 N. Y. 128; *Whitney Arms Co. v. Barlow*, 63 N. Y. 62; *Whitaker v. Masterton*, 106 N. Y. 277, 12 N. E. 604. Under a statute making directors liable for failure to file a report, the liability does not attach if a report is filed, though it may be false. *Bonnell v. Griswold*, 80 N. Y. 128; *Pier v. Hanmore*, 86 N. Y. 95; *Matthews v. Patterson*, 16 Colo. 215, 26 Pac. 812.

²⁷⁴ *Thacher v. King*, 156 Mass. 490, 31 N. E. 648. An indebtedness of a corporation to one of its directors constitutes a debt due within the statute. *Id.*

²⁷⁵ See *Rorke v. Thomas*, 56 N. Y. 559.

²⁷⁶ See *Cady v. Sanford*, 53 Vt. 632.

²⁷⁷ *Patterson v. Manuf'g Co.*, 41 Minn. 84, 42 N. W. 926.

²⁷⁸ *Garrison v. Howe*, 17 N. Y. 458; *Rorke v. Thomas*, 56 N. Y. 559; *Bruce v. Platt*, 80 N. Y. 381; *Cameron v. Seaman*, 69 N. Y. 396.

²⁷⁹ *Knox v. Baldwin*, 80 N. Y. 610.

²⁸⁰ *Sanborn v. Lefferts*, 58 N. Y. 179.

ery of a judgment against the company, of the debt, is not conclusive.²⁸¹

An action against a director by a creditor under these statutes is within the statute of limitations to recover a penalty. It is an action "upon the forfeiture."²⁸² The statute begins to run when the action accrues in favor of the creditor, as the fault on the part of the directors, as the fact.

By the weight of authority, such statutes have no extraterritorial effect, and the liability there is not enforced in another state.²⁸⁴

It also follows, from the penal character of these statutes, that there is no vested right in a cause of action arising from a judgment, and not only so, but that the right to bring an action before action has been commenced, but that the time before judgment, and an action prevented from being further prosecuted.²⁸⁵

²⁸¹ *Miller v. White*, 50 N. Y. 137. But see *C*

²⁸² *Merchants' Bank v. Bliss*, 35 N. Y. 412; *Knox v. Baldwin*, 80 N. Y. 610.

²⁸³ *Jones v. Barlow*, 62 N. Y. 202. Where a corporation becomes liable for a debt of the company because of its report, the right of action is barred after lapse of time (in New York, three years), though the default is committed before the report. See *Losee v. Bullard*, 79 N. Y. 404.

²⁸⁴ *Halsey v. McLean*, 12 Allen (Mass.) 438; *Law*, 166; *First Nat. Bank v. Price*, 33 Md. 166; *Prac. (N. S.)* 61; *Price v. Wilson*, 67 Barb. (N. Y.) 53; *Vt.* 632.

²⁸⁵ *Union Iron Co. v. Pierce*, 4 Biss. 327, *F* 327; *Lindauer*, 37 Mich. 217; *Knox v. Baldwin*, 80 Colo. 882.

CHAPTER XV.

FOREIGN CORPORATIONS.

- 246. Foreign Corporations Defined.
- 247-249. Status of a Foreign Corporation.
- 250-254. Actions by and against.
- 255. Visitorial Power over Foreign Corporations.

FOREIGN CORPORATIONS DEFINED.

246. A foreign corporation is a corporation created by or under the laws of another state or country.

Foreign corporations have been defined in a former chapter, in treating of the creation and citizenship of corporations.¹

STATUS OF A FOREIGN CORPORATION.

- 247. A corporation has the capacity to act and contract, by its agents, in a state or country other than that by which it was created, with the express or implied consent of that country or state.**
- 248. And by rules of comity, binding upon the courts of a state, foreign corporations have a right to do business therein, the consent of the state being presumed, except**
- (a) **Where it is prohibited by express statutory or constitutional enactment.**
 - (b) **Where to allow it to do so would be contrary to the public policy of the state.**
- 249. A state, if it sees fit, may, by legislation, exclude a foreign corporation altogether, or it may, subject to particular constitutional limitations, prescribe any conditions it may deem fit as a prerequisite to its**

¹ Ante, p. 74 et seq.

**right to do business with:
impose conditions in viol
stitution.**

Power to Act in Another Jurisdiction.

In *Bank of Augusta v. Earle*,² it was c
ing the powers conferred by the terms c
from the very nature of its being, can b
out of the limits of the state; that the
extraterritorial operation, and that, as a
ture of a law of the state, it can have n
in which that law operates; and that it
of making a contract in another place.
ruled this contention, and held that it
through its agents, with the consent of t
true," it was said, "that a corporation ca
of the boundaries of the sovereignty by
only in contemplation of law, and by forc
law ceases to operate, and is no longer o
have no existence. It must dwell in the
not migrate to another sovereignty. Bu
have its being in that state only, yet it c
that its existence there will not be recog
residence in one state creates no insuper
contracting in another. It is, indeed, a
and intangible; yet it is a person, for c
tion of law, and has been recognized as
court. * * * Now, natural persons
agents, are continually making contrac
do not reside, and where they are not
contract is made, and nobody has ever
agreements. And what greater objectio
of an artificial person, by its agents, t
scope of its limited powers in a sover
side, provided such contracts are per
the laws of the place?"

² 13 Pet. 519,

The question has been raised whether it is proper, as a matter of public policy, under any circumstances, for a state to recognize a corporation created by another state or a foreign government. The prosecution of a claim to property by an Alabama corporation in Louisiana was resisted in the latter state, in *Williamson v. Smoot*,³ on the ground that it was a violation of the sovereignty of a state, and prejudicial to the rights of its citizens, to recognize a corporation created by the legislature of another state. It was held, however, that though attempts directly opposed to the sovereign power of a state, or the rights of its citizens, made by a corporation deriving its existence from another state, ought to be repelled, yet where a corporation comes into the courts of a state other than that by which it was created, and there seeks to assert its rights, it ought to be recognized, and its rights ought to be enforced, where to do so would not prejudice the state or its citizens.⁴

It is well settled, according to the principle of these cases, that a corporation can, by its agents, go into another state than that by which it was created, and make any contract, or take any conveyance, that is within the powers conferred upon it by its charter, provided the state in which the contract or conveyance is made has not prohibited such a transaction, and the transaction is not contrary to the policy of its laws.⁵ And it is equally well settled, subject to the same limitations, that a corporation may maintain actions and enforce its rights in another state or country, if it does not seek to enforce claims contrary to its laws.⁶

³ 7 Mart. (La.) 34, 1 Cumming, Cas. Priv. Corp. 32.

⁴ And see *Blackstone Manuf'g Co. v. Inhabitants of Blackstone*, 13 Gray (Mass.) 488.

⁵ *Kennebec Co. v. Augusta Ins. & Banking Co.*, 6 Gray (Mass.) 204; *Hutchins v. Mining Co.*, 4 Allen (Mass.) 580; *Wright v. Lee*, 2 S. D. 596, 51 N. W. 708; *Reichwald v. Hotel Co.*, 106 Ill. 439; *Santa Clara Female Academy v. Sullivan*, 116 Ill. 375, 6 N. E. 183 (where it was held that a Wisconsin corporation could take lands by devise in Illinois); *Bard v. Poole*, 12 N. Y. 495 (where it was held that a Maryland corporation could make loans secured by mortgage on real estate in New York); *Merrick v. Van Santvoord*, 34 N. Y. 208; *Lancaster v. Improvement Co.*, 140 N. Y. 576, 35 N. E. 964 (where it was held that there was nothing in the laws of New York, or their general policy, to prohibit foreign corporations from acquiring land in the state).

⁶ Post, p. 634.

Though the rules of comity by which foreign corporations are recognized and their rights enforced are subject to local modification by the lawmaking power, until so modified they have the force of legal obligation. It is the duty of the courts to respect them until the legislature sees fit to modify them.⁷ This principle of comity is a part of our common law.⁸

Right to Exclude or to Impose Conditions.

A corporation created by one state or by a foreign government can exercise none of the functions or privileges conferred by its charter in any other state or country, except by the comity and consent of the latter. Any other state or country than that of its creation may exclude it altogether, if it sees fit, or it may impose such terms as it chooses as a condition of allowing it to do business.⁹ A corporation, as it has been expressed, "cannot migrate, but may exercise its authority in a foreign territory upon such conditions as may be prescribed by the law of the place."¹⁰ As was said in *Paul v. Commonwealth of Virginia*,¹¹ a "corporation, being the mere creature of a local law, can have no legal existence beyond the limits of the sovereignty where created. * * * The recognition of its existence, even by other states, and the enforcement of its contracts made therein, depend purely upon the comity of those states,—a comity which is never extended where the existence of the corporation or the exercise of its powers is prejudicial to their interests or repugnant to their policy. Having no absolute right of recognition in other states, but depending for such recognition and the enforcement of its contracts upon their assent, it follows, as a matter of course, that such assent may be granted upon such terms and conditions as those states may think proper to impose. They may exclude the foreign corporation entirely,

⁷ *Merrick v. Van Santvoord*, 34 N. Y. 208, 217.

⁸ *Elston v. Piggott*, 94 Ind. 17.

⁹ *Paul v. Virginia*, 8 Wall. 168; *Liverpool Ins. Co. v. Massachusetts*, 10 Wall. 566, 1 Cumming, Cas. Priv. Corp. 26; *Bank of Augusta v. Earle*, 13 Pet. 519, 585; *New York, L. E. & W. R. Co. v. Com.*, 129 Pa. St. 463, 18 Atl. 412; *Phenix Ins. Co. v. Burdett*, 112 Ind. 204, 13 N. E. 705; *Goldsmith v. Insurance Co.*, 62 Ga. 379; *People v. Fire Ass'n of Philadelphia*, 92 N. Y. 311; *Phoenix Ins. Co. v. Welch*, 29 Kan. 672; *State v. Phoenix Fire Ins. Co.*, 92 Tenn. 420, 21 S. W. 893; *Hartford Fire Ins. Co. v. Raymond*, 70 Mich. 485, 38 N. W. 474.

¹⁰ *Railroad Co. v. Harris*, 12 Wall. 65.

¹¹ 8 Wall. 168.

they may restrict its business to particular localities, or they may exact such security for the performance of its contracts with their citizens as in their judgment will best promote the public interest. The whole matter rests in their discretion."

The provision of the federal constitution that the citizens of each state of the Union shall be entitled to all the privileges and immunities of citizens in the several states does not require one state to recognize corporations created by another; for, though a corporation is to be regarded as a citizen for some purposes,¹² it is not a citizen within the meaning of that provision. "The privileges and immunities secured to citizens of each state in the several states by the provision in question are those privileges and immunities which are common to the citizens in the latter states, under their constitution and laws, by virtue of their being citizens. Special privileges enjoyed by citizens in their own states are not secured in other states by this provision. It was not intended by the provision to give to the laws of one state any operation in other states. They can have no such operation except by the permission, express or implied, of those states. The special privileges which they confer must therefore be enjoyed at home, unless the assent of other states to their enjoyment therein be given."¹³ Nor is a foreign corporation within the constitutional provision that "no state shall deny to any person within its jurisdiction the equal protection of its laws," so as to prevent a state from imposing conditions upon allowing it to do business.¹⁴

According to this principle, it is well settled that a state may impose a tax or license fee upon a foreign corporation, as a condition of allowing it to do business within its limits; and it can make no difference that a less tax, or no tax at all, is imposed upon domestic corporations engaged in the same business.¹⁵ Foreign corporations

¹² Ante, p. 24.

¹³ *Paul v. Virginia*, 8 Wall. 168. And see *Bank of Augusta v. Earle*, 18 Pet. 519, 585; *Pembina Con. Silver Mining & Milling Co. v. Pennsylvania*, 125 U. S. 181, 8 Sup. Ct. 737; *Norfolk & W. R. Co. v. Pennsylvania*, 136 U. S. 114, 10 Sup. Ct. 958; *Ducat v. City of Chicago*, 48 Ill. 172; *Tatem v. Wright*, 23 N. J. Law, 429.

¹⁴ *Pembina Con. Silver Mining & Milling Co. v. Pennsylvania*, *supra*; *Norfolk & W. R. Co. v. Pennsylvania*, *supra*; ante, p. 24.

¹⁵ *Liverpool Ins. Co. v. Massachusetts*, 10 Wall. 566, 1 Cumming, Cas. Priv. Corp. 26; *Pembina Con. Silver Mining & Milling Co. v. Pennsylvania*, 125 U. S. 181, 8

merce into or through another state, the latter cannot exclude it; for this would be an interference with interstate commerce, in violation of the constitutional grant to congress of the exclusive power to regulate commerce, and of the acts of congress on the subject.²⁰ For instance, a state statute requiring a foreign corporation to file a certificate, or observe any other condition, before bringing an action for goods sold and delivered in the state, but made at its place of business in another state, or before otherwise making contracts in the state for carrying on commerce between the states, would be void as an interference with interstate commerce.²¹ The same is true of a statute imposing a tax upon foreign corporations as a condition of their being allowed to transport goods into or through the state.²² This provision of the constitution includes telegraph corporations engaged in transmitting messages from a point in one state to a point in another.²³

A state has the absolute right to entirely exclude a foreign corporation from its territory, or, having given it a license to do business within the state, to revoke it, in its discretion, for good cause, or

²⁰ *Paul v. Virginia*, 8 Wall. 168.

²¹ *Ante*, p. 225; *Cooper Manuf'g Co. v. Ferguson*, 113 U. S. 727, 5 Sup. Ct. 739; *Kindel v. Lithographing Co.*, 19 Colo. 310, 35 Pac. 538; *Ware v. Shoe Co.*, 92 Ala. 145, 9 South. 136; *Cook v. Brick Co.*, 98 Ala. 409, 12 South. 918; *Robbins v. Taxing Dist.*, 120 U. S. 489, 7 Sup. Ct. 592; *Bateman v. Milling Co.*, 1 Tex. Civ. App. 90, 20 S. W. 931; *Pickard v. Car Co.*, 117 U. S. 34, 6 Sup. Ct. 635. A state law imposing a tax on foreign corporations doing business in the state, based on the amount of capital used by the corporation in such state, is not an interference with commerce. *People v. Wemple*, 131 N. Y. 64, 29 N. E. 1002.

²² See *Indiana v. American Exp. Co.*, 7 Biss. 227, Fed. Cas. No. 7,021. In *Crutcher v. Kentucky*, 141 U. S. 47, 11 Sup. Ct. 851, a Kentucky statute requiring the agent of a foreign express company doing business in the state to pay a license fee of five dollars, and deposit with the auditor a statement of the company's assets and liabilities, showing that it has an actual capital of at least \$150,000, was held unconstitutional, as an interference with interstate commerce, in so far as it applied to companies transporting goods between points in the state and points in other states, although they also transported between points in the state. And see *Norfolk & W. R. Co. v. Pennsylvania*, 136 U. S. 114, 10 Sup. Ct. 958; *McCall v. California*, 136 U. S. 104, 10 Sup. Ct. 881.

²³ *Pensacola Tel. Co. v. Western Union Tel. Co.*, 96 U. S. 1; *Telegraph Co. v. Texas*, 105 U. S. 460; *Ratterman v. Telegraph Co.*, 127 U. S. 411, 8 Sup. Ct. 1127; *Leloup v. Port of Mobile*, 127 U. S. 640, 8 Sup. Ct. 1380.

without any cause at all. And its motion for a writ of habeas corpus is denied. The corporation has no constitutional right to do business in any other state than that of its incorporation. Its exclusion therefrom violates no constitutional provision. *Continental Ins. Co.*²⁴ the legislature of the state may, if any foreign insurance company should attempt to do business against it from the state courts to the effect that it should upon become the duty of the secretary of the state to do business within the state. It was not held that it should be granted to restrain the revocation of the provision, though a state has no right to exclude foreign corporations from the federal courts where they have jurisdiction. The power to exclude foreign corporations belongs to the state, and the means by which it accomplishes that result are a proper subject of judicial inquiry.

Such a statute, however, cannot prevent a suit from being moved into the federal courts.²⁵ A statute which permits a corporation to do business in the state as a condition precedent to the granting of a license shall be granted, the statute is void, and a corporation could not be prosecuted for violating it.

A state, of course, has a perfect right to regulate the operations of a particular class, and exclude from that class those which it sees fit, discriminate between corporations and individuals.

It seems to have been held, in effect, that the admission of corporations organized for the purpose of doing business, it impliedly excludes corporations organized for other purposes; and it has been held that corporations organized for a particular purpose, the state does not admit a foreign corporation for that purpose specified, and also for other purposes.

With the question of the expediency of imposing conditions upon foreign corporations, the question is purely a legislative question to do. It is purely a legislative question.

²⁴ 94 U. S. 535.

²⁵ *Insurance Co. v. Morse*, 20 Wall. 445.

²⁶ *Barron v. Burnside*, 121 U. S. 186, 7 S.

²⁷ *Isle Royale Land Corp. v. Secretary of S*



unless it is plainly in conflict with some constitutional provision; and, if there is doubt as to its constitutionality, the doubt must be resolved in favor of the legislature.²⁸ "It has repeatedly been held—and there seems to be no conflict of authority—that corporations of one state have no right to exercise their franchises in another state, except upon the assent of such other state, and upon such terms as may be imposed by the state where their business is to be done. The conditions imposed may be reasonable or unreasonable. They are absolutely within the discretion of the legislature."²⁹

Foreign Corporations in Fraud of the Laws of a State, or Contrary to its Policy.

The courts of a state will not recognize as valid a corporation organized in fraud of its laws in another state, or a corporation of another state which is contrary to the policy of its laws.³⁰ In some states the laws for the formation of corporations are more favorable than in others, and, for this reason, residents of a state sometimes go into another state and form a corporation under its laws for the purpose of doing business in the state of their residence. Whether such corporations will be recognized as valid in the state of the corporators' residence depends upon whether the incorporation is to be regarded as an evasion of and fraud upon its laws. Some courts seem to have held that the mere fact that residents of a state go into another state and form a corporation for the purpose of doing business in the state of their residence is an evasion of the laws of the state in which they are incorporated, and a fraud upon such laws.³¹ But, by the better opinion, there must be something more than this to make out a case of fraud upon the laws of either state. There must be some express prohibition against such an incorporation, or else the general policy of the laws must be against it. The question arose in New York in *Demarest v. Flack*.³² In this case the defendants,

²⁸ *Phenix Ins. Co. v. Burdett*, 112 Ind. 204, 13 N. E. 705; *State v. Carey*, 2 N. D. 36, 49 N. W. 164; *State v. Phoenix Ins. Co.*, 92 Tenn. 420, 21 S. W. 893.

²⁹ *Hartford Fire Ins. Co. v. Raymond*, 70 Mich. 485, 38 N. W. 474, 482.

³⁰ *Hill v. Beach*, 12 N. J. Eq. 31; *Land Grant Railway & Trust Co. v. Board Co. Com'rs Coffey Co.*, 6 Kan. 245; *Carroll v. City of East St. Louis*, 67 Ill. 568; *Demarest v. Flack*, 128 N. Y. 205, 28 N. E. 645.

³¹ *Hill v. Beach*, 12 N. J. Eq. 31.

³² 128 N. Y. 205, 28 N. E. 645. And see, to the same effect, *Lancaster v. Im*.

residents of New York, had formed a corporation in West Virginia for the purpose of doing business there as a foreign corporation. The plaintiff, a resident of New York, seeking to hold the corporation liable, contended (1) that these facts rendered the incorporation invalid, so far, at least, as it concerned its citizens; or, (2) that the facts rendered it a question for the determination of the jury whether the incorporation was attempted to be effected for mere evasion and in fraud of the laws of New York, and that, if the jury should find that the incorporation was invalid, the corporation would be void. The court held that the laws of both states permitted incorporation, and that this corporation had been formed; that the liability from personal liability would be as great as the security of creditors would not be affected by incorporation under the laws of New York. West Virginia plainly favored the formation of corporations composed of nonresidents, the purpose to be done outside the state; and that the court should recognize foreign corporations formed for business there,—held that the incorporation was valid in West Virginia and in New York. The court also held that the incorporation was not an attempted evasion of the laws of New York, and should not be submitted to the jury as a question of fact.³³

provement Co., 140 N. Y. 576, 35 N. E. 964, where the court held that the laws of New Jersey to do business in New York.

³³ In regard to the latter point, it was said by the court. "we might find different juries come to different conclusions on the same facts, and we should have a corporation in one view a jury might take of such facts. One plaintiff's satisfaction of one jury, and another plaintiff's dissatisfaction of another jury, thus we should have a corporation as to A., and not as to B., the same question constantly arising as often as the corporation is sued. This would be intolerable. It must be submitted to the jury whether it has business dealings, or as to none. It is a question of law, instead of fact."



A foreign corporation will not be recognized in a state if it is contrary to the policy of its laws, as where the laws expressly or impliedly prohibit corporations of its character, or a corporation for such purposes.²⁴ It was held by the Illinois court that a corporation created by the laws of Connecticut for the sole purpose of buying and selling lands had no power to purchase and hold lands in Illinois, as it was against the general policy of the laws of that state on the subject of domestic corporations, and would tend to create perpetuities.²⁵

Retaliatory Statutes.

In some of the states what are known as "retaliatory statutes" have been enacted, the object being to prevent other states from imposing greater burdens and restrictions upon corporations of the state by which the statute is enacted than are imposed by that state upon corporations of such other states. Thus, in Illinois it is provided that whenever the existing or future laws of any state shall require of insurance companies incorporated under the laws of Illinois, and having agencies in such other state, any deposit, or the payment of any tax, license fee, etc., greater than the amount required for such purposes for similar companies by the then existing laws of Illinois, then all companies of such state establishing or having an established agency in Illinois shall be required to pay to the auditor, for taxes, license fees, etc., an amount equal to the amount required by the laws of such other state.²⁶ And in many states there are statutes in effect providing generally that foreign corporations shall not exercise any privileges in the state which are not accorded by the state by which they are created to similar foreign corporations.²⁷ Such statutes

²⁴ Land Grant Railway & Trust Co. v. Board Co. Com'rs Coffey Co., 6 Kan. 245; Carroll v. City of East St. Louis, 67 Ill. 568.

²⁵ Carroll v. City of East St. Louis, *supra*.

²⁶ This law becomes operative upon the enactment by the other state of the law with the additional requirements, and it is immaterial that there are no Illinois corporations doing business in such state. Germania Ins. Co. v. Swigert, 128 Ill. 237, 21 N. E. 530; State v. Fidelity & Casualty Co., 77 Iowa, 648, 42 N. W. 509. But see State v. Insurance Co., 49 Ohio St. 440, 31 N. E. 658.

²⁷ See State v. Western Union Mut. Life Ins. Co., 47 Ohio St. 167, 24 N. E. 392, and other cases cited in the preceding and following notes.

as these are valid, unless they violate some particular provision of the state constitution.³⁸

A foreign corporation which has complied with the local laws should not, as a measure of retaliation, under a retaliatory statute, be excluded from doing business in the state upon the ground that the laws of the state by which it was created would exclude foreign corporations from doing business there under like conditions, unless it is clear that such is the effect of the law. Rules of comity require that doubt in such a case should be resolved in favor of the corporation.³⁹

What Constitutes "Doing Business" in the State.

Questions have frequently arisen as to what constitutes "doing business" in the state, within the meaning of the statutes relating to foreign corporations, and the answer is not always clear. If a foreign corporation continuously does any substantial part of its business in the state, however little, it is within the statute. Clearly, it does business in the state if it has an office and sells some of its goods there.⁴⁰ And by the better opinion a single act of its ordinary business brings it within the statute. Thus, a corporation organized for the purpose of lending money on real-estate mortgage security does business by making a single loan and taking a mortgage to secure it.⁴¹ In like manner an insurance company would do business in the state by issuing a single policy of insurance.⁴² Such acts constitute the ordinary business of the company.

The supreme court of the United States has held that a statute or constitutional provision prohibiting a foreign corporation from doing "any business" in the state until it has complied with the conditions imposed contemplates carrying on or continuing business in

³⁸ *People v. Fire Ass'n of Philadelphia*, 92 N. Y. 311; *Home Ins. Co. v. Swigert*, 104 Ill. 666; *State v. Insurance Co. of North America*, 115 Ind. 257, 17 N. E. 574; *Talbott v. Casualty Co.*, 74 Md. 536, 22 Atl. 395.

³⁹ *State v. Fidelity & C. Ins. Co.*, 39 Minn. 538, 41 N. W. 108; *State v. Insurance Co.*, 49 Ohio St. 440, 31 N. E. 658.

⁴⁰ *People v. Wemple*, 131 N. Y. 64, 29 N. E. 1002; *People v. Horn Silver Min. Co.*, 105 N. Y. 76, 11 N. E. 155.

⁴¹ *Farrior v. Security Co.*, 88 Ala. 275, 7 South. 200; *Ginn v. Security Co.*, 92 Ala. 135, 8 South. 388.

⁴² *Lamb v. Lamb*, 6 Biss. 420, Fed. Cas. No. 8,018.

the state, and does not apply to a single act of business, though it may be done as a part of the ordinary business of the company, and that a foreign manufacturing company, for instance, may come into the state and make a single sale without bringing itself within the statute.⁴³ This ruling was not necessary to dispose of the case, for the transaction was within the protection of the provision of the federal constitution prohibiting the states from interfering with interstate commerce, and two of the justices based their concurrence in the judgment on this ground alone. The decision does not seem to be sound, particularly as the statute expressly prohibited "any" business. It is, in effect, adding to the statute. If it is followed, the logical result will be to allow a foreign investment or insurance company to come into a state and make a loan, or issue a policy of insurance. If they can do so once, when they do not intend to do so again, they may come back a second time, and a third. To bring a foreign corporation within the statute, must it be shown that it intended to do business regularly for a week or a month or a year? And, if a foreign corporation comes into a state with the intention of engaging regularly in business there, does it come within the statute if it does only a single act of business, and then determines not to do more? If the decision referred to is to be followed, where can the line be drawn? The only way to carry out the intention of the legislature in enacting these statutes—and that is the extent of the court's duty—is to give effect to the terms used according to their ordinary meaning. And when the legislature says that a foreign corporation shall not "do any business," it should be taken to mean what the language plainly imports,—that it shall not "do any" business. Such is the construction placed upon a similar statute by the Alabama court, which held that a foreign loan company brought itself within the statute by making a single loan in the state.⁴⁴

Such statutes as these are evidently intended only to prohibit a foreign corporation from doing any part of its ordinary business in the state. It does not prohibit an act not in the way of its ordinary business. Thus, they could not be construed as preventing an action by a foreign corporation on an insurance policy issued by a do-

⁴³ *Cooper Manuf'g Co. v. Ferguson*, 113 U. S. 727, 5 Sup. Ct. 739.

⁴⁴ Note 41, *supra*.

mestic corporation, where the only bus the state related to the policy;⁴⁵ nor a ration from making a purchase of machi ported to and set up in the state of venting a foreign trust company from railroad company in the state, and takin to secure them;⁴⁷ nor as prohibiting a cepting notes in the state for the price in another state.⁴⁸

The prosecution or defense of an act the state, within the meaning of such corporation do business in the state l goods to factors in the state, for sale by of subscriptions to the capital stock of within the statutes.⁵¹ Nor does the sta a foreign corporation, where the agreem other state, and the securities were do there.⁵² Many similar decisions might

⁴⁵ *Tabor v. Manufacturing Co.*, 11 Colo. 419, 1

⁴⁶ *Colorado Iron Works v. Sierra Grande Min.*

⁴⁷ *Gilchrist v. Railroad Co.*, 47 Fed. 593. See St. 119.

⁴⁸ *Fuller & J. Manuf'g Co. v. Foster*, 4 Dak.

⁴⁹ *Utley v. Mining Co.*, 4 Colo. 369; *Powder F Mont.* 145, 22 Pac. 383; *Christian v. Mortgage Call v. Mortgage Co.*, 99 Ala. 427, 12 South. App. 92, 21 S. W. 687; *St. Louis, A. & T. F* 18 S. W. 43; *Fuller & J. Manuf'g Co. v. Foste*

⁵⁰ *Bertha Zinc & Mineral Co. v. Clute* (Com.

⁵¹ *Payson v. Withers*, 5 Biss. 269, Fed. Cas. 1

⁵² *Scruggs v. Mortgage Co.*, 54 Ark. 566, 16 S. Ann. 516, 9 South. 104.

⁵³ A contract made by a citizen of Indiana through an agent of the company in Indiana, v was sustained because made, not with the agen *Lamb v. Bowser*, 7 Biss. 815, Fed. Cas. No. 8, 8,000. And see, to the same effect, *Hyde v. Northwestern Mut. Life Ins. Co. v. Elliott*, 5 Fe

Effect of Noncompliance with Conditions.

The statutes imposing conditions upon foreign corporations vary in the different states, and even where they are similar the courts do not agree in construing them, and as to the effect of contracts and transactions in violation of their terms. In all cases the object is to ascertain the intention of the legislature, and when the intention is ascertained it must be given effect.

Some statutes merely prohibit foreign corporations from doing business in the state, or from acquiring, holding, and disposing of property in the state, until they have filed a copy of their charter or articles of incorporation, or performed the other conditions that may be imposed, but do not attach any penalty, or say what shall be the consequences of noncompliance. Some of the courts hold that such a statute does not render contracts or transactions by foreign corporations before compliance with its terms void, but that the corporation merely renders itself subject to exclusion at the instance of the public authorities.⁵⁴ This view does not commend itself. It makes the statute virtually a dead letter. The weight of authority is to the effect that all contracts entered into in violation of the statute are absolutely void. No other penalty being attached, this is the only effective way of enforcing the prohibition.⁵⁵

⁵⁴ Washburn Mill Co. v. Bartlett, 3 N. D. 138, 54 N. W. 544; Wright v. Lee, 4 S. D. 237, 55 N. W. 931. And see Slauson v. Schwabacher, 4 Wash. 783, 31 Pac. 329.

⁵⁵ In re Comstock, 3 Sawy. 218, Fed. Cas. No. 3,078; Cincinnati Mut. Health Assur. Co. v. Rosenthal, 55 Ill. 85; Lycoming Fire Ins. Co. v. Wright, 55 Vt. 526; Rising Sun Ins. Co. v. Slaughter, 20 Ind. 520; Hoffman v. Banks, 41 Ind. 1; Farmers' & Merchants' Ins. Co. v. Harrah, 47 Ind. 236; Union Cent. Life Ins. Co. v. Thomas, 46 Ind. 44; Bank of British Columbia v. Page, 6 Or. 435; Aetna Ins. Co. v. Harvey, 11 Wis. 395; Reliance Mut. Ins. Co. v. Sawyer, 160 Mass. 413, 36 N. E. 59; National Mut. Fire Ins. Co. v. Pursell, 10 Allen (Mass.) 232; Jones v. Smith, 3 Gray (Mass.) 500; Neuchatel Asphalt Co. v. Mayor, etc. (Com. Pl.) 30 N. Y. Supp. 252; Barbor v. Boehm, 21 Neb. 450, 32 N. W. 221; Northwestern Mut. Life Ins. Co. v. Elliott, 5 Fed. 225. "When the legislature prohibits an act," said the Illinois court, "or declares that it shall be unlawful to perform it, every rule of interpretation must say that the legislature intended to interpose its power to prevent the act, and, as one of the means of prevention, that the courts shall hold it void. This is as manifest as if the statute had declared that it should be void. To hold otherwise would be to give to the person or corporation or individual the same rights in enforcing prohibited contracts as the good citizen who

Some of the statutes not only prohibit doing business before compliance with their terms, but also impose a penalty for their violation, and others impose a penalty without express prohibition. Some courts hold that the legislature, by annexing a specific penalty, manifests an intention that the penalty shall be exclusive, and that contracts made before compliance with the statute are valid.⁵⁶ Most of the courts, however, hold that the annexation of a penalty renders all acts which subject the party to the penalty unlawful, and therefore unenforceable, under the generally accepted rules⁵⁷ that, where a statute prohibits an act and attaches a penalty, it renders the act unlawful, and that attaching a penalty without express prohibition is an implied prohibition.⁵⁸ If the statute is not in terms prohibitory, and the penalty is imposed as a tax, and for purposes of revenue, and not by way of punishment, it does not prohibit contracts before compliance with its terms.⁵⁹

Where a statute, as is sometimes the case, merely requires foreign corporations to file a copy of their charter, or observe other requirements, within a certain time after commencing business in the state, and imposes a penalty upon their officers or agents if they fail to do so, it has been held that it is not to be construed as prohibiting continuance of business after such failure, so as to avoid their contracts, the only penalty incurred being the penalty imposed by the statute.⁶⁰

respects and conforms to the law. To permit such contracts to be enforced, if not offering a premium to violate a law, it certainly withdraws a large portion of the fear that deters men from defying the law. To do so places the person who violates the law on an equal footing with those who strictly observe its requirements." *Cincinnati Mut. Health Assur. Co. v. Rosenthal*, *supra*.

⁵⁶ *Toledo Tie & Lumber Co. v. Thomas*, 33 W. Va. 566, 11 S. E. 37; *Columbus Ins. Co. v. Walsh*, 18 Mo. 229; *Union Mut. Life Ins. Co. v. McMillen*, 24 Ohio St. 67; *Harris v. Runnels*, 12 How. 79; *Edison General Electric Co. v. Canadian Pac. Nav. Co.*, 8 Wash. 370, 36 Pac. 260; *La France Fire Engine Co. v. Town of Mt. Vernon*, 9 Wash. 142, 37 Pac. 287, and 38 Pac. 80.

⁵⁷ *Clark*, *Cont.* 386.

⁵⁸ *Dudley v. Collier*, 87 Ala. 431, 6 South. 304; *Buxton v. Hamblen*, 82 Me. 448; *Thorne v. Insurance Co.*, 80 Pa. St. 15; *Cary-Lombard Lumber Co. v. Thomas*, 92 Tenn. 587, 22 S. W. 743.

⁵⁹ See *Larned v. Andrews*, 106 Mass. 435.

⁶⁰ *Northwestern Mut. Life Ins. Co. v. Overholt*, 4 Dill. 287, Fed. Cas. No. 10,338; *Kindel v. Lithographic Co.*, 19 Colo. 310, 35 Pac. 538; *Slauson v. Schwabacher*, 4

It is held that a statute forbidding any foreign corporation to do business in the state until it has complied with the conditions prescribed, and imposing a penalty for its violation, but which imposes no duty or prohibition upon persons dealing with a corporation which has not complied with the law, does not render its contracts void as to such persons, so as to prevent them from maintaining an action thereon. For instance, it is held that a policy of insurance issued by a foreign insurance company, which has not complied with the law so as to be entitled to do business in the state, may nevertheless be enforced by the assured. Some courts base this rule on the ground that the corporation is estopped to set up its noncompliance with the law to escape liability on its contracts.⁶¹ Others base it upon the ground that the statute is intended for the protection of persons dealing with the corporation, and that the legislature did not intend to avoid its contracts to their prejudice.⁶²

Estoppel.

If a corporation does business in another state without complying with the conditions precedent imposed by the state, it cannot escape liability on contracts made by it on the ground that it was not qualified to do business in the state. It is estopped to set up such a defense. It was so held by Judge Caldwell where a life insurance company set up such a defense to defeat an action on a policy issued by it. "By the fact of doing business in the state," he said, "it asserted a compliance with the laws of the state, and after enjoying all the benefits of that business, and receiving the money of the assured, it will not be heard to say that it never submitted 'to the jurisdiction of the state.' It can reap no advantage from its own wrong."⁶³ And the estoppel extends to agents and members of the corporation who participate in the unauthorized transactions.⁶⁴

Wash. 788, 81 Pac. 829; *Whitman Agricultural Co. v. Strand*, 8 Wash. 647, 36 Pac. 682.

⁶¹ See following paragraph.

⁶² *Pennypacker v. Insurance Co.*, 80 Iowa, 56, 45 N. W. 408; *Union Mut. Life Ins. Co. v. McMillen*, 24 Ohio St. 67; *The Manistee*, 5 Blm. 332, Fed. Cas. No. 9,027; *Ehrman v. Insurance Co.*, 1 Fed. 471.

⁶³ *Berry v. Indemnity Co.*, 46 Fed. 439. And see *Ehrman v. Insurance Co.*, 1 Fed. 471.

⁶⁴ *Kilgore v. Smith*, 122 Pa. St. 48, 15 Atl. 698.

Some of the courts hold that, if a foreign corporation makes a contract which is within the powers conferred upon it by its charter, the other party cannot escape the obligations imposed upon him by the contract, nor dispute the rights of the corporation under it, on the ground that it had not complied with the law imposing conditions upon its right to do business in the state; the corporation being regarded as in the position of a *de facto* corporation, whose contracts are valid, the state only having the right to object, or else the other party being held to be estopped to dispute the validity of the contract.⁶⁵ Other courts take the position that the statute is based upon grounds of public policy, and the contract, being prohibited, is illegal and void, and that the doctrine of estoppel does not extend so far as to enable a person or corporation to do in effect what is forbidden by law. And they therefore hold that in such a case the other party to the contract is not estopped to show the illegality of the contract for the purpose of preventing a recovery upon it.⁶⁶

In *Fitts v. Palmer*,⁶⁷ a statute of Colorado expressly declared that no foreign corporation should purchase or hold real estate in the state, except as provided in the statute. The supreme court held that the failure of a foreign corporation to comply with the statute did not render a conveyance to it void, so that it might be attacked collaterally by a private person. This decision is against the weight

⁶⁵ See ante, p. 86, as to *de facto* corporations. *Sherwood v. Alvis*, 83 Ala. 115, 3 South. 307. In this case the defendant had obtained a loan from a foreign corporation engaged in lending money in Alabama, and had given a mortgage to secure the same. In an action by the purchaser at a sale under the mortgage for possession, the defendant contended that the mortgage was void because the corporation had no known place of business, or authorized agent, within the state, as required by law. It was held that he was estopped to set up such a defense. For other decisions in support of the test, see *Wright v. Lee*, 2 S. D. 596, 51 N. W. 706; *Washburn Mill Co. v. Bartlett*, 3 N. D. 138, 54 N. W. 544. And see *American Loan & Trust Co. v. East & West R. Co.*, 37 Fed. 242; *La France Fire Engine Co. v. Town of Mt. Vernon*, 9 Wash. 142, 37 Pac. 287; *Rathbone, Sard & Co. v. Frost*, 9 Wash. 162, 37 Pac. 298.

⁶⁶ In *re Comstock*, Fed. Cas. No. 3,078; *Williams v. Cheney*, 3 Gray (Mass.) 222; *National Mut. Fire Ins. Co. v. Pursell*, 10 Allen (Mass.) 232; *Rising Sun Ins. Co. v. Slaughter*, 20 Ind. 520; *Cincinnati Mut. Health Assur. Co. v. Rosenthal*, 55 Ill. 90; *Aetna Ins. Co. v. Harvey*, 11 Wis. 895.

⁶⁷ 132 U. S. 282, 10 Sup. Ct. 93

of decisions in the state courts.⁶⁶ And Mr. Justice Miller "earnestly" dissented.

Powers of Foreign Corporation—Limitation of Charter.

The rule of comity by which a corporation is permitted to do business in another state than that by which it was created does not change its nature as a foreign corporation, or give it any powers which are not given by its charter. Nor does it exempt persons who deal with it from the effect of legislation by the state or country of its creation under power reserved under its law. "Though permitted to come into the local jurisdiction, and there exercise its powers, for the accomplishment of the purposes of its creation, it remains essentially a foreign corporation. It derives its vitality, its corporate capacity, its very life, from the law of its origin. Comity adds to it no new function, or greater powers than are bestowed upon it by its charter. That, being the instrument of the company's creation, and prescribing the limits of its legal existence, must exert the most obvious influence upon all its transactions; and, whether abroad or at home, it can do nothing which does not fairly fall within the scope and purpose of that instrument."⁶⁷ And persons dealing with a foreign corporation must take notice of the limitations in its charter, and also of the power over it reserved to the state or country to which it owes its being, and they are bound accordingly.⁷⁰ "Wherever a corporation goes for business, it carries its charter, as that is the law of its existence, and the charter is the same abroad that it is at home. Whatever disabilities are placed upon the corporation at home it retains abroad, and whatever legislative control it is subjected to at home must be recognized and submitted to by those who deal with it elsewhere."⁷¹

⁶⁶ See cases in note 66, *supra*.

⁶⁹ Wm. L. Murfree, Esq., in note to *Republican Silver Mines v. Brown*, 7 C. A. 419.

⁷⁰ *Canada S. Ry. Co. v. Gebhard*, 100 U. S. 527, 537, 3 Sup. Ct. 363, 369; *Hoyt v. Thompson's Ex'r*, 19 N. Y. 207; *Metropolitan Bank v. Godfrey*, 23 Ill. 579, 609; *Manhattan Life Ins. Co. v. Fields* (Tex. Civ. App.) 26 S. W. 280. If the charter of a corporation, or the general laws of the state of its creation, prohibit certain contracts, as contracts between it and its officers or employees, the prohibition applies to contracts in another state. *Rue v. Railway Co.*, 74 Tex. 474, 8 S. W. 533.

⁷¹ *Canada S. Ry. Co. v. Gebhard*, *supra*.

If a foreign corporation whose existence is not disputed has made a contract in a manner that it is made amenable to suit by it, and a suit is brought against it in that manner, it is not necessary for the plaintiff, at the time of filing the suit, to show that the corporation has the power under its charter to make contracts.

The rules recognized in some states corporation cannot plead ultra vires to contract, and that the corporation is estopped by an action brought against it, apply to a borrower from a foreign corporation, to defeat an action by the corporation on a loan on the ground that the corporation had no authority to make the loan.⁷³ As we have seen, the effect of ultra vires contracts.⁷⁴

Same—Limitations of the Local Law

It does not follow, even when a corporation is a citizen of a state, that it can exercise all the powers conferred upon it by its charter. Its powers also depend upon the laws of the state in which they are exercised. In other words, a corporation is subject not only by its charter and the laws of the state in which it is organized, but also by the laws of the state in which it exercises its powers. If a state prohibits corporations from exercising their power in this respect, the laws of that state apply to corporations. And generally, in the absence of a treaty or statute to the contrary, the rule, a foreign corporation cannot exercise its powers in a state unless the local laws allow to similar domestic corporations.

If the charter of a corporation prohibits it from doing business in another state, though the statute in the latter state, for a prohibition, a corporation cleaves to it everywhere.

72 McCluer v. Railroad, 13 Gray (Mass.)

78 *Pancoast v. Insurance Co.*, 79 Ind. 172 (N. Y.) 378.

⁷⁴ Ante, p. 170.

⁷⁵ *Runyan v. Coster's Lessee*, 14 Pet. 12
67 Ill. 568; *White v. Howard*, 46 N. Y. 144

76 White v. Howard, 88 Conn. 842, 1 Cu

that a statute of wills of one state, since it has no extraterritorial effect, cannot prevent a corporation of that state from taking by devise in another state, where there is no such prohibition.¹⁷ This decision would seem to be a sound one, but the contrary has been held in Illinois.¹⁸ Where the laws of a state prohibit a corporation from taking land by devise, a devise in that state to a foreign corporation is void, though by its charter, and by the laws of the state of its creation, it is authorized to take by devise.¹⁹

Corporations de Facto.

A foreign corporation will be accorded the status of a corporation de facto, if it is a corporation de facto in the state by which it was created, and if it has complied with the law relating to foreign corporations. In such a case, persons who deal with it cannot attack its corporate existence on the ground of irregularity in organization. Any question affecting its right to transact business because of such irregularity is a matter of inquiry only for the state of its creation.²⁰

Rights and Immunities of Members.

The rights and immunities of members of foreign corporations are within the rule of comity, and must be respected. They cannot be held individually liable, for instance, for the debts or torts of the corporation, unless they are made so by its charter, or by some statute.²¹

Quo Warranto and Mandamus.

Quo warranto is a proper remedy, unless excluded by statute, to try the right of a foreign corporation to carry on business in the state, and to oust it if it is without right.²² The executive officers of the state, in issuing certificates to foreign corporations under the statutes,

¹⁷ *Id.*

¹⁸ *Starkweather v. Society*, 72 Ill. 50.

¹⁹ *White v. Howard*, 46 N. Y. 144.

²⁰ *Lancaster v. Improvement Co.*, 140 N. Y. 576, 35 N. E. 964; *Bank of Toledo v. International Bank*, 21 N. Y. 542.

²¹ *Merrick v. Van Santvoord*, 34 N. Y. 208.

²² *State v. Fidelity & Casualty Ins. Co.*, 39 Minn. 538, 41 N. W. 106; *State v. Fidelity & Casualty Ins. Co. (Ohio Sup.)* 31 N. E. 658; *State v. Western Union Mut. Life Ins. Co.*, 47 Ohio St. 167, 24 N. E. 392; *State v. Fidelity & Casualty Ins. Co.*, 77 Iowa, 648, 42 N. W. 509.

Where the executive officer of the state granting and revoking permits for foreign do business in the state is required to go conditions exist, and is not vested with damus will lie to compel him to grant a But if he is invested with discretionary quired to grant a permit when he "is sat curities, investments," etc., of the corpo where he is given the power to revoke (after an examination, he "has reason to made by a foreign corporation is false, his by mandamus."⁵

250. By the comity of states, a corporation is bound to obey the laws of one state or country as well as the laws of another state or country, even though they conflict, if the application of the laws of the other state or country does not conflict with its own.

251. A foreign corporation cannot be sued in a state, unless jurisdiction is obtained by service within the state upon the corporation. This provision is very generally made in the laws of the states upon particular officers or agents of the corporation doing business in the state. The corporation which does business within a state is deemed to have submitted to the jurisdiction of the courts of that state impliedly by its doing business there.

252. A judgment recovered against a foreign corporation after due service of process on the corporation in the state is entitled, under the comity of states, to be enforced in another state.

253. A judgment recovered against a foreign corporation after due service of process on the corporation in the state is entitled, under the comity of states, to be enforced in another state.

²² *State v. Carey*, 2 N. D. 36, 49 N. W. 16; *Wilder*, 40 Kan. 561, 20 Pac. 285.

laws of the United States, to the same faith and credit in all other states as in the state in which it was rendered.

254. For the purposes of jurisdiction of actions in the federal courts, a corporation is a "citizen" or "inhabitant" of the state of its creation, and of that state only.

Actions by Foreign Corporations.

It is well settled that, by the law of comity among nations, a corporation created by one sovereignty may assert its rights by suit in the courts of another sovereignty, and the same rule of comity prevails among the states of this Union.⁸⁶

Actions against Foreign Corporations.

Formerly it was held that a foreign corporation could not be sued for the recovery of a personal demand outside of the state by which it was chartered. The principle that a corporation must dwell in the place of its creation, and cannot migrate to another sovereignty, coupled with the doctrine that an officer of the corporation does not carry his functions with him when he leaves the state, so as to render service of process upon him service upon the corporation, prevented personal actions against it. There was no mode of compelling its appearance in the foreign jurisdiction.⁸⁷ With the growth of corporations, the doctrine of the exemption of foreign corporations from suit caused much inconvenience and injustice, and to obviate this the legislatures of the several states interposed, and provided for service of process upon officers and agents of foreign corporations

⁸⁶ *Bank of Augusta v. Earle*, 13 Pet. 519; *British American Land Co. v. Ames*, 6 Metc. (Mass.) 391; *Portsmouth Livery Co. v. Watson*, 10 Mass. 91; *Cone Export & Commission Co. v. Poole*, 41 S. C. 70, 19 S. E. 208; *Diamond Match Co. v. Roeber*, 106 N. Y. 473, 13 N. E. 419; *St. Louis, A. & T. Ry. Co. v. Fire Ass'n*, 55 Ark. 163, 13 S. W. 43; *Emerson v. Machine Co.*, 51 Mich. 5, 16 N. W. 182; *Portsmouth Livery Co. v. Watson*, 10 Mass. 91; *Henriques v. Dutch West India Co.*, 2 Ld. Raym. 1532; *Silver Lake Bank v. North*, 4 Johns. Ch. (N. Y.) 370.

⁸⁷ Per Mr. Justice Field, in *St. Clair v. Cox*, 106 U. S. 350, 1 Sup. Ct. 354, 357. See *McQueen v. Manufacturing Co.*, 16 Johns. (N. Y.) 5; *Peckham v. Inhabitants*, 16 Pick. (Mass.) 274, 286.

doing business therein. These statutes, as we have seen, are valid, for a state has a right to impose conditions upon allowing a foreign corporation to do business. If a foreign corporation comes into a state in which there is such a law, and transacts business there, it impliedly submits to the jurisdiction of the state, and will be bound accordingly. "The state may," said Mr. Justice Field in *St. Clair v. Cox*,⁸⁸ "impose as a condition upon which a foreign corporation shall be permitted to do business within her limits, that it shall stipulate that, in any litigation arising out of its transactions in the state, it will accept as sufficient the service of process on its agents or persons specially designated, and the condition would be eminently fit and just. And such condition and stipulation may be implied as well as expressed. If a state permits a foreign corporation to do business within her limits, and at the same time provides that, in suits against it for business there done, process shall be served upon its agents, the provision is to be deemed a condition of the permission; and corporations that subsequently do business in the state are to be deemed to assent to such condition as fully as though they had specially authorized their agents to receive service of process."⁸⁹

By the weight of authority, statutes to the contrary notwithstanding, service upon a person as the agent of a foreign corporation will be binding upon the corporation only when such person represents the corporation. The mere fact that the person upon whom service is made is an officer of the corporation does not render the service equivalent to service upon the corporation, so as to give the court jurisdiction over it. He must be in the state as the representative of the corporation. If a corporation should send an agent into another state to make contracts there on its behalf, service on him in an action on a contract so made, in accordance with the laws of the state, would bind the corporation.⁹⁰ But if an officer of the cor-

⁸⁸ 106 U. S. 350, 1 Sup. Ct. 354, 360.

⁸⁹ And see *Lafayette Ins. Co. v. French*, 18 How. 404; *Colorado Iron Works v. Sierra Grande Min. Co.*, 15 Colo. 499, 25 Pac. 325; *Baltimore & O. R. Co. v. Gallahue's Adm'r*, 12 Grat. (Va.) 655; *Railroad Co. v. Harris*, 12 Wall. 65; *Moulin v. Insurance Co.*, 24 N. J. Law, 222, 25 N. J. Law, 57; *Wilson v. Fire-Alarm Co.*, 149 Mass. 24, 20 N. E. 318; *Day v. Bank*, 13 Vt. 97, 101; *Gibbs v. Insurance Co.*, 63 N. Y. 114; *Emerson v. Machine Co.*, 51 Mich. 5, 16 N. W. 182.

⁹⁰ See cases above cited.

poration should go into the state, not as the representative of the corporation, but on business of his own, service on him would not bind the corporation, either in the state or in the federal courts.⁹¹

This is the well-settled rule of the federal courts, and of most of the state courts, but it is not fully recognized by all of the state courts. In New York it is provided that personal service of the summons upon a foreign corporation in an action for a cause arising in the state may be made by delivering a copy thereof, within the state, to the president, secretary, or treasurer, or a director thereof; and it is held that it is not necessary that the officer served shall be in the state in his official capacity, or engaged in the business of the corporation, nor that the corporation shall have property, or do business, or have a place of business, in the state.⁹²

If a foreign corporation has property so situated within the limits of a state, and under its jurisdiction, that it may be attached by the ordinary process of law, a suit may be there maintained against the corporation by an attachment of the property, as it might against a foreign individual having property so situated, though a personal judgment could not be rendered against the corporation.⁹³

Effect of Judgment against Foreign Corporation.

A judgment recovered against a foreign corporation after due service of process on an authorized agent in the state is entitled, under the constitution and laws of the United States, to the same faith and credit in all other states as in the state in which it was rendered.⁹⁴ A judgment against a corporation in one state can always be attacked in another state by showing that the court acquired no jurisdiction to render a personal judgment against it. And, to sustain a personal judgment against a foreign corporation, there must have been personal service upon an authorized agent within the state, or a voluntary ap-

⁹¹ *Newell v. Railway Co.*, 19 Mich. 336; *St. Clair v. Cox*, 106 U. S. 350, 1 Sup. Ct. 354; *Moulin v. Insurance Co.*, 24 N. J. Law, 222, 224; *Good Hope Co. v. Railway Barb Fencing Co.*, 22 Fed. 635; *Bentliff v. Finance Corp.*, 44 Fed. 667; *Golden v. Morning News*, 42 Fed. 112; *State v. District Court of Ramsey Co.*, 26 Minn. 233, 2 N. W. 608.

⁹² *Hiller v. Railroad Co.*, 70 N. Y. 223; *Pope v. Manufacturing Co.*, 87 N. Y. 137.

⁹³ *Blackstone Manuf'g Co. v. Inhabitants of Blackstone*, 13 Gray (Mass.) 488.

⁹⁴ *Lafayette Ins. Co. v. French*, 18 How. 404.

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*Jurisdiction of Federal Courts in
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** St. Clair v. Cox, 106 U. S. 350, 1 Sup.

** 106 U. S. 350, 1 Sup. Ct. 354.

*7 Ante, p. 74, and cases there cited. See
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S. 221, 16 Sup. Ct. 273; Day v. India-Ru
nelly v. Cordage Co., 66 Fed. 613; Gorhu
-418; Miller v. Manufacturing Co., 46 Fed.



quently been applied, though not always uniformly, in determining the jurisdiction of the federal courts of suits against corporations. Formerly the judiciary act required suits, with certain exceptions, to be brought in the district whereof the defendant might be an inhabitant, or in which he might be "found." Under this provision it was held that a corporation could be sued in a state other than that of its creation, if it carried on business there, and had an agent there, in compliance with a state statute, upon whom process could be served. Under such circumstances it was "found" there, though not an inhabitant.⁸⁸ In 1887 the judiciary act was changed by omitting the last clause. And the present act provides that a civil suit before a circuit or district court must be brought in the district of which the defendant is an inhabitant, except when the jurisdiction is founded only on the fact that the action is between citizens of different states, in which case suit may be brought in the district of the residence of either the plaintiff or the defendant. Under this statute a suit in the federal courts against a corporation, where the ground of federal jurisdiction is the diverse citizenship of the parties, may be brought either in the district of which the corporation is an inhabitant, or in the district wherein the plaintiff resides. In all other cases the suit must be brought in the district of which the corporation is an inhabitant; and a corporation is not a citizen, inhabitant, or resident of any state, within the meaning of this provision, other than that by which it was created, though it may do business and have an agent in other states, and may have submitted in other states to the jurisdiction of the state courts.⁸⁹

This provision, in terms, applies only to so much of the jurisdiction of the circuit courts of the United States as is "concurrent with the courts of the several states," and as concerns cases in which the matter in dispute exceeds \$2,000 in value. It applies to trade-mark cases,

⁸⁸ *Ex parte Schollenberger*, 96 U. S. 369; *Knott v. Insurance Co.*, Fed. Cas. No. 7,894; *Fonda v. Assurance Co.*, Id. 4,904.

⁸⁹ *In re Keasbey & Mattison Co.*, 160 U. S. 221, 16 Sup. Ct. 273; *Southern Pac. Co. v. Denton*, 146 U. S. 202, 13 Sup. Ct. 44; *Shaw v. Mining Co.*, 145 U. S. 444, 12 Sup. Ct. 935, 2 Cumming, Cas. Priv. Corp. 5, *Shep. Cas. Corp.* 55, *W. D. Smith, Cas. Corp.* 15; *Filli v. Railroad Co.*, 37 Fed. 65. *Contra*, *Miller v. Mining Co.*, 45 Fed. 345; *U. S. v. Southern Pac. R. Co.*, 49 Fed. 297; *Shainwald v. Davids*, 69 Fed. 704.

for here there is concurrent jurisdiction. cases, however, in which exclusive jurisdiction courts, and without regard to the amount held that the provision does not apply, a corporation may be sued in any district in which it is located.¹⁰¹ The statute does not apply to suits created by a foreign government, of any state, and they may be sued in any court served with process.¹⁰²

VISITORIAL POWER OVER FOREIGN CORPORATIONS

255. The courts of a state have no jurisdiction over foreign corporations, nor over their internal affairs.

This, as a general proposition, is well settled. Jurisdiction belongs solely to the courts of the state in which the corporation was created. And no such jurisdiction can be conferred on the courts of a state by a statute subjecting the business in the state to actions in its courts. A state cannot enforce a forfeiture of the franchise for violation of law, or removal of the corporation. And can they exercise authority over the corporation or the relations between the corporation and the state out of, and depending upon, the law of the state?

¹⁰⁰ In re Keasbey & Mattison Co., 160 U. S. 100.

¹⁰¹ This point seems not to have been finally settled, but there is dictum in support of the text, as regards the decisions of the supreme court, In re Hohorst, 150 U. S. 653, 14 Sup. Ct. 221; In re S. 221, 16 Sup. Ct. 273; Smith v. Manufacturing Button Works v. Wade, 72 Fed. 298. Corbett v. Fed. 613; Gorham Manuf'g Co. v. Watson Signal Co. v. Hall Signal Co., 65 Fed. 625.

¹⁰² In re Hohorst, 150 U. S. 653, 14 Sup. Ct. 221.

¹⁰³ North State Copper & Gold Min. Co. v. Wilkins v. Thorne, 60 Md. 253.



it has been held that they cannot entertain an application of a stockholder of a foreign corporation, even though he be a resident of the state, for a writ of mandamus to compel the corporation to annul a forfeiture of his stock, and reinstate him as a stockholder;¹⁰⁴ nor a suit to enjoin a foreign corporation from paying a stock dividend, upon the ground that it has no authority to declare such a dividend;¹⁰⁵ nor a suit to appoint a receiver generally, and not merely of the assets within the state;¹⁰⁶ nor a suit by a stockholder to compel a distribution of assets;¹⁰⁷ nor a suit by a former member of a foreign mutual insurance company to compel it to restore him to his rights under a policy issued to him in the state where the corporation was created.¹⁰⁸

But it has been held that this doctrine does not prevent the courts of a state from issuing a writ of mandamus, upon application of a stockholder, to compel the resident president of a foreign corporation doing business in the state to allow an inspection of books of the corporation in his possession;¹⁰⁹ nor from entertaining an action by a stockholder to compel a foreign corporation doing business in the state to issue to him a new or duplicate stock certificate in place of one which has been lost or destroyed.¹¹⁰

The dissolution of a corporation, whether by the expiration of its charter, the forfeiture of its privileges, or as the result of its insolvency, is governed and controlled by its charter and the law of the sovereignty by which it was created. A court of one state or country, therefore, has no jurisdiction of a suit to dissolve a corporation created by the laws of another state or country.¹¹¹ Local courts of

¹⁰⁴ *North State Copper & Gold Min. Co. v. Field*, 64 Md. 151, 20 Atl. 1039. But see *Guilford v. Telegraph Co.*, 59 Minn. 332, 61 N. W. 324.

¹⁰⁵ *Howell v. Railway Co.*, 51 Barb. (N. Y.) 378.

¹⁰⁶ *Stafford v. Mills Co.*, 13 R. I. 310.

¹⁰⁷ *Redmond v. Manufacturing Co.*, 13 Abb. Prac. N. S. (N. Y.) 332.

¹⁰⁸ *Smith v. Insurance Co.*, 14 Allen (Mass.) 336.

¹⁰⁹ *State v. Swift* (Del. Super.) 30 Atl. 781. And see *State v. McCullough*, 3 Nev. 202. But see *People v. Parker Vein Coal Co.*, 10 How. Prac. (N. Y.) 543.

¹¹⁰ *Guilford v. Telegraph Co.*, 59 Minn. 332, 61 N. W. 324.

¹¹¹ Note by Wm. L. Murfree, 7 C. C. A. 421; *Republican Mountain Silver Mines v. Brown*, 7 C. C. A. 412, 58 Fed. 644.

equity, however, will take jurisdiction of the assets of a foreign corporation which may be within the state, in case of the dissolution or insolvency of the corporation, and see to their equitable distribution.¹¹²

¹¹² Note, 7 C. C. A. 421; *Smith v. Insurance Co.*, 8 Tenn. Ch. 502, 6 Lea (Tenn.) 564; *Leipold v. Marony*, 7 Lea (Tenn.) 128; *Patterson v. Lynde*, 112 Ill. 196; *Barclay v. Talman*, 4 Edw. Ch. (N. Y.) 123; *Day v. Telegraph Co.*, 66 Md. 354. 7 Atl. 608.

Clk.Pr.Corp.—41

APPENDIX

THE LOGICAL CONCEPTION

One of the most notable features of as a concrete branch of human knowledge is the diversity between the definitions, proper to the term "corporation." Perhaps the cause of this diversity is that the complex elements of a corporation are not capable of being compressed into a definition, that is, which satisfies the demand that it shall include all the qualities that are essential to the thing, and that distinguish it from other institutions.

To fulfill this requirement, by presenting a definition of a corporation with greater elaboration than are found in standard text-books, is of no interest of clear thought, even if it be of practical application. The foundation of a corporation is visible and tangible elements of all conditions, words, which are patent to every observer, whether in law or not, and which characterize the thing as composed of more than one individual. Added, in logical order, the several essential qualities distinguish corporations as a species of institution between municipal and commercial entities, both of which are called "corporations," that by a logical analysis that pretends to unity and mi-

¹ A paper read before the West Virginia State Bar meeting in Huntington, W. Va., Nov. 11, 1908, at the Charleston, West Virginia, bar, and published by the author.

ject of the following essay, therefore, is confined to the modern business corporation, or incorporated joint-stock company.

A corporation is an association of individuals—formed under the sanction of the state—for the accomplishment of a distinct and definite purpose. These three phrases represent the essential elements of a corporation; elements, that is, which exist in every conceivable corporation, and which, when existing in corporations, differ materially from the same elements as they exist in a number of other institutions recognized by the law. To acquire an adequate and distinct notion, therefore, of the meaning of the term “corporation,” requires an analysis of each of these elements.

I. A complete conception of “an association of individuals” as such involves the consideration of (a) its origin, (b) the mode of its existence, and (c) its dissolution; and also of the relations of the several individuals composing it to the body itself and to each other. In these particulars the association which constitutes a corporation differs from other associations known to the law.

(a) While the corporation has its origin in an agreement between individuals, and to this extent resembles a partnership, incorporation becomes effective only through the operation of a special charter or a general enabling act, whose provisions, respectively, are accepted by the execution of the agreement.

(b) The only material element in the mode of existence of an association, considered as merely existing, is the period of time for which it endures. Herein is found the most striking diversity between corporations and all other associations, to wit, a perpetual and unending existence, either actual or potential. This capacity is laid down as the very *raison d'être* of corporations by the older common-law writers. And, though modern statutes very generally prescribe a limit to the life of corporations organized under them, the principles upon which their perpetuity was based, and the means whereby it was effected, are in no wise altered.

Obviously, the fatal obstacle to the continuity of the association in and of itself is the mortality of its individual members, for, both in nature and in law, the death of a single member of an unincorporated association works a dissolution of that particular association. To overcome this obstacle requires the capacity to supply new members, who shall fill the precise positions of those who die or resign

or otherwise sever the connection. This capacity to constitute new members, upon whom are cast, by mere operation of law, all the rights and liabilities of those to whom they succeed in respect of the corporate enterprise, is what is meant by the legal term "perpetual succession,"—a quality ascribed to corporations by the common law as their essential and distinguishing characteristic. The resulting corporate "identity," in spite of changes in component parts, means simply the persistence unchanged, in point of proportion or remedy, of all rights and liabilities existing between the several members of the association, and between them and third persons. While the conception of this identity seems so simple and natural in the light of this analysis, it seems to have involved no little difficulty in the minds of the old common lawyers, and to have given birth to the "artificial person," who lived and moved and had his being in that nebulous region, the "contemplation of law," and to whom were ascribed such a bewildering array of "invisible," "intangible," and "immortal" qualities.

(c) The dissolution of the association in question may be voluntary or involuntary. In so far as it may be effected by the consent of its members, or may be enforced in invitum at the instance of creditors or a portion of its members, the principle on which it is based and the mode of its operation differ little from those obtaining in respect of unincorporated associations. The distinguishing feature in this element is found in the power of the state, inherent in some instances, expressly reserved in others, to enforce a dissolution, by way of penalty, for a variety of unlawful acts.

In addition to these essential elements of the association as a body, the matter of organization naturally suggests itself; but, as these elements may exist independent of any organization, the latter is more logically considered in connection with the purpose for which the corporation is formed. An adequate and distinct conception of a corporation as "an association of individuals," therefore, may be completed by briefly considering these individuals as members of one association. The particulars which distinguish them from members of unincorporated associations involve the consideration of (a) the mode of becoming members, (b) the mode of severing their connection with the association, and (c) the rights and liabilities incident to such membership.

(a, b) The method and effect of constituting individual members of the association by execution of the articles of incorporation, or by original subscriptions to the capital stock, vary little from those incident to the formation of a partnership. The distinctive feature of the corporation in this respect, and one of the most important of all its qualities, is found in the effect of assignment of outstanding shares of its capital stock. Upon such an assignment, the assignee is, by operation of law, invested with all the rights and subjected to all the liabilities of the original stockholder; and that without regard to the dissent of the other associates, and in defiance of the common-law maxim, where it still obtains, that choses in action are not assignable. Furthermore, when the stock assigned is fully paid, the assignor, in the absence of fraud or collusion, is at once relieved of all liabilities, either to his former associates or to third persons, in respect of the corporate enterprise. The requirement that the transfer shall be in good faith is material only when statutes impose on stockholders an individual liability for corporate debts, in excess of the amount of unpaid stock held by them.

(c) The preceding paragraph exhibits the distinctive mode of terminating the individual's membership in the association. As his death has no other effect, as to him or his estate, than in the case of all other associations, it remains briefly to analyze the rights and liabilities incident to a continuing membership. This involves their general nature and limitations, and the several parties concerned therein.

The rights and liabilities of members of an incorporated association are such only as grow out of the proper object and purpose of the corporation, and their subject-matter is confined strictly to their respective shares of the corporate property or funds. This latter principle, which is peculiar to corporations as distinguished from unincorporated associations, imposes a strict limitation on the liability of members to creditors of the corporation, and constitutes at the present day one of the most important qualities of such associations. While these broad propositions may be subject to certain exceptions under the law as to ultra vires acts and official misconduct, they are involved in the essential nature of corporations; and this analysis does not aim to include exceptions declared by positive rules of law in matters of detail.

The other parties to the rights and member include: First. The association organized body; he having a right, on shall proceed to carry out the objects and shall not divert the corporate funds the other, being liable to it for unpaid any special duties imposed on him by members. And, third, creditors and tion of these two classes is of minor relations between them are usually association, as a body, is a party; and dent to them are usually enforceable rate. In general, each individual is liable burdens so far as they are imposed third persons, individual members may rights which the corporate management while, by statute, individual liability extent is imposed in specific instances tial feature of all the relations into which the fact of incorporation is that the corporate enterprise and the corporation

II. The second element, which is one is that the association of the individual sanctioned by the state, which sanctions to its form and operation.

The sanction which arises from general liabilities, and providing means for it share with unincorporated associations from the latter by an express act of tion, emanating from the lawmaking assumes the form of a special charter appears as a general enabling act, concerning who bring themselves within its provisions or the other, this express legislative into a corporation the association of by mutual agreement on their part.

As just indicated, the operation



itiative from the execution of the articles of incorporation. Its subsequent operation and effect involve all the powers and duties which devolve upon the corporation and its component parts. The continuance of its operation depends upon its twofold nature: First, as a grant of corporate power, from whose exercise peculiar rights arise; and, second, as a law, which prescribes the form and mode in which those powers are to be exercised and the resulting rights enforced. As to the latter, it is, in general, subject to repeal and amendment like any other law. As to the former, it, for many purposes, constitutes a contract, which the state cannot alter except by virtue of certain powers inherent in it upon grounds of public policy, or by the force of special reservations to which the associates have assented, expressly or by implication. It is this contract feature, and the rights thence arising under the federal constitution, that distinguish the legal sanction given to a corporation from the recognition accorded unincorporated associations.

III. The last element in the suggested analysis of a corporation is the distinct and definite purpose for whose accomplishment the association is formed by its members, and sanctioned by the state. It is foreign to the purpose of such analysis to discuss the several objects for which a corporation may be formed, and the kinds of business it may carry on. For this involves the economic, rather than the legal, aspect of the institution; and, moreover, it is not a matter which will serve to separate corporations from other associations. It is expressly enacted in many of the states, indeed, that a corporation may carry on any business for which a partnership may be formed, though they are generally prohibited from dealing in real estate.

The material thing to be noted in this connection is that the peculiar corporate powers exist only for the purpose of carrying out the object expressed in the charter, and, when they are pushed beyond that limit, they, in theory, suffer paralysis. While it is true that in some instances liabilities, enforceable by third persons, may be incurred by acts beyond the range of the corporate enterprise, this result betokens no extension of corporate powers, but it inures only by way of estoppel, operating on the individuals who compose the association. The same acts, done or threatened, entitle any or

all the members to sue to prevent their continuance, and in many cases render the corporation liable to forfeiture of its charter at the instance of the state.

So much being premised as to the nature of the corporate enterprise, it remains to consider how it is to be carried out, and the analysis of this third element is complete. Having regard still to what is peculiar to and distinctive of corporations, it may be said that the forces set in motion to this end are (a) the corporate powers, while the instruments with which they work are (b) the corporate funds.

(a) Subject to the limitations heretofore noted as growing out of the object of the corporation, and those hereafter stated in connection with their mode of exercise, the legal powers of a corporation are those of a natural person. It can properly, of course, have no rights save those of property, as distinguished from those of the person; nor can it be subject to any liability except in respect to its property. But, within these limits, rights and remedies, both for and against it, exist, as in the case of the natural man. The form and mode of exercising these powers, and the management of the corporate funds, exhibit the greatest diversity between corporations and other institutions known to the law; for they are the logical consequences of the very nature and objects of the association. The exercise of these corporate powers may be considered (1) as to its substance, and (2) as to its form.

(1) The separate existence and concurrent operation of the mental intent and the physical act which must combine to give rise to legal rights and liabilities are admirably illustrated in the valid acts of a corporation. The corporation is composed of all the stockholders, and the intent to engage in a given transaction must proceed from them. In the event that unanimous consent cannot be secured for a given course, it is the rule of natural equity as well as positive law that the will of the majority shall have effect as the will of the whole. But the contract must be executed, or other thing done, by an individual agent or agents; and, in deference to this necessity, the general corporation law provides for, and recognizes, directors and other officers, who are empowered to carry on the general business of the corporation, and whose acts in that regard bind all the stockholders.

(2) In respect of form in the exercise of the corporate powers in accordance with the principles above indicated, the first requisite is to determine and register the will of the majority. This is required to be done by appropriate means, at a meeting of stockholders, called with prescribed formalities, and attended by such a number of them as the charter declares to be a quorum. The majority may express their consent that a specific act shall be done, or, after it is done, be held valid; or that consent may be implied from the appointment of general officers or agents, within the scope of whose powers and duties that act lies.

The forms under which the mandates of the corporation are carried out by its officers and agents must, of course, be appropriate to the subject-matter. But the law has been particular to prescribe the evidence which must be adduced to show that the act was done as the act of the corporation, to wit, the corporate name and seal. While the corporate name and the corporate seal were formerly universally included among the elements that are of the essence of the corporation, and while Blackstone says that the name "is the very being of its constitution," it would seem that their sole function is the same as that of the name of an individual; i. e. to identify the corporation in respect to its rights and liabilities. Though necessary forms, they are none the less mere forms, and the use of the seal is nowadays necessary, in general, only when its use would be required in the case of a natural person.

A brief consideration of the origin and disposition of the corporate funds will give an adequate conception of this last, but most important, element of a modern business corporation. The nucleus of the property of the corporation is found in the capital stock subscribed by the original stockholders. A specified proportion of this is generally required to be paid in before the incorporation takes effect; and the subscriber is liable to the corporation, and also to its creditors under certain conditions, for so much of his subscription as remains unpaid. It is to this capital stock, paid and unpaid, that the peculiar rules of corporation law apply; for profits actually accruing thereon may be applied, in general, as a majority of the stockholders see fit, subject always to limitations growing out of the nature of the corporate business.

The rights of management and disposition of property which ac-

crue to a natural person by reason of his ownership are limited, so far as they concern corporate funds, by two principles, the effect of both of which is to dedicate them unalterably to certain purposes. The first is that, inasmuch as the capital stock was subscribed and paid for the accomplishment of a definite object, any person who owns a share therein is entitled to object to its diversion from that object, and to insist that it shall be applied to its accomplishment, unless that is impossible. The state has a similar right when the object is one which concerns the public, and the corporate powers were conferred for the purpose of effecting it. The second is that inasmuch as creditors contract upon the credit of the capital stock, and have, in general, no recourse when that is exhausted, they have the right to resist any diversion of the fund from the proper objects of the corporation, to the prejudice of their right to be paid their just claims.

The foregoing is submitted as a logical statement of all the elements essential to a modern business corporation, with such analysis of each as is necessary to differentiate a corporation from all other associations known to law, as regards that particular. It aims to include all that is necessary, and nothing that is unnecessary, to that end.

While no mention is made herein of the nature and effect of ultra vires acts and official misconduct, it may be explained that the object sought is to exhibit the anatomy of a healthy corporation, without regard to diseases and mishaps to which it may be exposed.

It seems worth while to attempt to embody a clear conception of a corporation—"immortality," "corporate identity," "perpetual succession," and all—without any aid from the "artificial person" whom Coke and Blackstone regarded so lovingly, and who is such a bugbear to, at least, one modern text writer. Whether this attempt has been worth while, it must be left for the reader to judge.

In conclusion, the whole matter may be presented in the form of a chart, by means of which the logical division of the subject and the connection of its several parts may be seen at a glance. (See following page.)

A CORPORATION IS

A BODY OF INDIVIDUALS—	FORMED UNDER THE SANCTION OF THE STATE—	FOR A DISTINCT AND DEFINITE PURPOSE—
Origin: Mutual agreement. Acceptance of charter. Mode of existence: Continuity: Perpetual succession. Corporate identity.	Form in which sanction is expressed: Special charters. General enabling act. Conditions precedent to sanction: Filling articles of agreement. Subscribing stock. Operation of sanction: As embodying legal rules: Repeal and amendment. As grant of corporate powers: Obligation of contract. Right to alter or repeal: Inherent power. Express reservation.	What purposes lawful Chartered purpose exclusive. Means and method of effecting it. Corporate powers: General nature. Form of exercise: Acts of majority. Officers and agents. Name and seal. Effect of exceeding powers. Corporate funds: Whence derived. Capital. Profits. Management and control: Ultimate object sought. Limitation upon: Public. Shareholders. Creditors.
Dissolution: Voluntary. Involuntary. At instance of state. Of creditors and shareholders. Individual members: Mode of becoming such. Original subscribers. Assignees of stock. How and when connection ceases. Assignment of stock. Rights and liabilities. Limited to corporate purpose and funds. Other parties thereto.		

TABLE OF CASES

[THE FIGURES REFER

A	
Abbey v. Dry Goods Co., 596.	Am
v. Long, 604.	4'
Abbott v. Hapgood, 118.	Am
v. Packet Co., 172.	C
v. Refining Co., 92, 104, 110.	Am
v. Smelting, etc., Co., 57.	F
Aberdeen Ry. Co. v. Blakie, 511, 512.	Am
Adams v. Milling Co., 609.	Am
Adams & Westlake Co. v. Deyette, 146,	
153.	An
Adderly v. Storm, 584, 585.	An
Addlestone Linoleum Co., in re, 372.	C
Adler v. Manufacturing Co., 592.	Am
Aetna Ins. Co. v. Harvey, 626, 629.	Am
Aetna Nat. Bank v. Charter Oak Life	Am
Ins. Co., 148.	Am
Agate v. Sands, 604.	Am
Agricultural Branch R. Co. v. Winches-	Am
ter, 331, 450.	Am
Albany N. R. Co. v. Brownell, 217.	Am
Albert v. Bank, 172, 429, 430.	Am
Alexander v. Searcy, 400.	Am
Allen v. Curtis, 391, 393, 401, 505, 535.	Am
v. Fairbanks, 606.	Am
v. Railroad Co., 321, 411, 438, 439,	Am
526, 559.	Am
v. Wilson, 394, 395, 399.	Am
v. Woonsocket Co., 150.	Am
Allibone v. Hager, 276, 292.	Am
Alling v. Wenzel, 373.	Am
v. Wenzell, 510.	Am
Allis v. Jones, 161.	Am
American Asylum v. President, Direct-	Am
ors, etc., of Phoenix Bank, 29.	Am
American Building & Loan Ass'n v.	Am
Rainbolt, 290, 303, 331.	Am
American Cent. Ry. Co. v. Miles, 532.	Am
American Exp. Co. v. Patterson, 139.	Am
American File Co. v. Garrett, 586.	Am
American Homestead Co. v. Linigan,	Am
100, 107.	Am
American Live-Stock Commission Co. v.	Am
Chicago Live-Stock Exch., 255.	Am
American Loan & Trust Co. v. East &	Am
West R. Co., 629.	Am
v. Minnesota & N. W. R. Co., 92.	Am
American Mortg. Co., of Scotland v.	Am
Tennille, 168.	Am
American Nat. Bank v. American	Am
Wood-Paper Co., 146.	Am
v. Oriental Mills, 421.	Am
Clk. Pr. Corp.	(658

[The figures refer to pages.]

Ashton v. Burbank, 448.
 Ashuelot Boot & Shoe Co. v. Hoit, 265.
 Ashuelot R. Co. v. Elliot, 214, 218.
 Ashurst's Appeal, 400.
 Asiatic Banking Corp., In re, 151.
 Aspinwall v. Daviess County Com'rs, 22.
 Astor v. New York Arcade Ry. Co., 87, 45.
 Astoria & S. C. R. Co. v. Hill, 310.
 Athol Music Hall Co. v. Carey, 266-268, 270.
 Atkins v. Albree, 356.
 Atkinson v. Railroad Co., 46, 89.
 Atlantic City Waterworks Co. v. Consumers' Water Co., 47.
 Atlantic Cotton Mills v. Abbott, 301, 309.
 v. Indian Orchard Mills, 503.
 Atlantic De Laine Co. v. Mason, 465.
 Atlantic Mut. Fire Ins. Co. v. Sanders, 465, 491.
 Atlantic & O. R. Co. v. Sullivan, 89.
 Atlantic & P. R. Co. v. City of St. Louis, 48.
 Attorney General v. Bay State Mining Co., 617.
 v. Chicago & N. W. R. Co., 46, 219.
 v. Garrison, 248.
 v. Great Northern Ry. Co., 248.
 v. Hanchett, 56, 63.
 v. Jamaica Pond Aqueduct Corp., 248.
 v. Joy, 44, 48.
 v. Lorman, 57, 69.
 v. McArthur, 46, 47.
 v. Mercantile Marine Ins. Co., 22.
 v. North America Life Ins. Co., 44, 45, 210.
 v. Simonton, 29.
 v. Stevens, 91, 247.
 v. Tudor Ice Co., 247.
 v. Utica Ins. Co., 247.
 Atwood v. Merryweather, 393.
 Auburn Bolt & Nut Works v. Shultz, 268.
 Auburn Opera-House & P. Ass'n v. Hill, 311.
 Auerbach v. Mill Co., 176.
 Aultman v. Waddle, 100.
 Aultman's Appeal, 584.
 Aurora A. & H. Soc. v. Paddock, 142, 487, 500.
 Australian Royal Mail Steam Nav. Co. v. Marzetti, 158.
 Ayers v. Banking Co., 163.

B

Bacon v. Insurance Co., 146, 147, 172.
 v. Irvine, 395.
 v. Railroad Co., 196.
 v. Robertson, 250, 392.
 Bagg's Case, 52.
 Bagnall v. Carlton, 117.
 Bailey v. Bancker, 589.
 v. Gaslight Co., 393.

Bailey v. Hollister, 217, 587.
 v. Mayor, 81.
 v. Trustees of Lincoln Academy, 84.
 Baines v. Babcock, 593, 597.
 Baker v. Backus' Adm'r, 62, 237, 243.
 v. Fales, 28.
 Bakersfield Town Hall Ass'n v. Chester, 55.
 Bakewell v. Board, 29.
 Balch v. Hallet, 356.
 v. Wilson, 604.
 Baldwin v. Canfield, 7, 8, 420, 489.
 Baltimore City Pass. Ry. Co. v. Humbleton, 359.
 Baltimore & D. P. R. Co. v. Pumphrey, 222.
 Baltimore & O. R. Co. v. Gallahue's Adm'r, 25, 78, 635.
 v. Harris, 75, 80.
 v. Koontz, 76.
 Baltimore & P. R. Co. v. Fifth Baptist Church, 195.
 Banet v. Railroad Co., 324, 325, 327, 450, 451.
 Banigan v. Bard, 363, 364.
 Bank v. Lanier, 407, 413, 459.
 Bank of Alabama v. Gibson's Adm'r, 30.
 Bank of Attica v. Manufacturers' & Traders' Bank, 407, 421, 457.
 Bank of Augusta v. Earle, 76, 490, 613, 615, 616, 634.
 Bank of Batavia v. New York, L. E. & W. R. Co., 438, 526.
 Bank of British Columbia v. Page, 626.
 Bank of Chillicothe v. Swayne, 175.
 Bank of Circleville v. Renick, 243.
 Bank of Columbia v. Patterson's Adm'r, 157, 158, 483.
 Bank of Commerce v. McGowan, 227.
 Bank of Commerce's Appeal, 251, 421.
 Bank of Ft. Madison v. Alden, 390.
 Bank of Genesee v. Patchin Bank, 150.
 Bank of Holly Springs v. Pinson, 458.
 Bank of Louisville v. Gray, 352.
 Bank of Manchester v. Allen, 84.
 Bank of Michigan v. Niles, 140, 187.
 Bank of Middlebury v. Rutland & W. R. Co., 400.
 Bank of Montreal v. J. E. Potts Salt & Lumber Co., 554.
 Bank of Niagara v. Johnson, 236.
 Bank of Poughkeepsie v. Ibbotson, 596, 597.
 Bank of St. Mary's v. St. John, 607.
 Bank of Shasta v. Boyd, 101.
 Bank of South Carolina v. Gibbs, 80.
 Bank of Toledo v. City of Toledo, 202, 227.
 v. International Bank, 88, 632.
 Bank of U. S. v. Dandridge, 53.
 v. Davis, 502.
 v. Deveau, 75, 76.
 v. Dunn, 495, 497.
 v. Lyman, 85.
 v. Planters' Bank, 29, 30.
 Bank of Utica v. Mengher, 84.
 Bank of Vincennes v. State, 240.

[The figures refer to pages.]

- Banks v. Pôitiaux**, 168.
Barbor v. Boehm, 626.
Barclay v. Talman, 236, 641.
Bard v. Poole, 614.
Bardstown & L. R. Co. v. Metcalfe, 142, 144.
Barker, In re, 475, 479.
 v. Insurance Co., 156.
Barned's Banking Co., In re, 151.
Barnes v. Hall, 259.
 v. Suddard, 168.
Barr v. Glass Co., 514.
 v. New York, L. E. & W. R. Co., 378, 511, 513.
 v. Plate-Glass Co., 511.
Barrick v. Gifford, 572, 579, 596-598, 602.
Barron v. Burnside, 619.
 v. Palne, 559, 592, 600.
Barrow v. Turnpike Co., 168.
Barry v. Exchange Co., 142, 145, 146, 256.
Barstow v. Mining Co., 428, 429.
Bartlett v. Drew, 540, 542, 563, 564, 593.
Barton v. Association, 236, 445.
Barwick v. Bank, 196.
Bash v. Mining Co., 93, 95.
Bashford-Burmister Co. v. Agua Fria Copper Co., 68, 107.
Basshor v. Dressel, 48.
Bateman v. Milling Co., 618.
 v. Railway Co., 147.
Bates v. Coronado Beach Co., 150.
 v. Insurance Co., 351.
 v. Lewis, 305.
 v. Railroad Co., 160.
 v. Wilson, 58, 96, 107.
Bathe v. Society, 528.
Battelle v. Pavement Co., 113-115, 514.
Bavington v. Railroad Co., 300, 319.
Bayless v. Oure, 245.
Beach v. Bank, 194.
 v. First Methodist Episcopal Church, 269.
 v. Miller, 511, 608, 609.
 v. Smith, 315, 316.
Beal v. Bank, 584.
Bean v. Trust Co., 434, 440, 442.
Becher v. Mill Co., 420.
Beckett v. Houston, 317.
Beebe v. Power Co., 143.
Beer Co. v. Massachusetts, 208, 209, 211, 213.
Beers v. Spring Co., 343, 348, 352, 353.
Beggs v. Illuminating Co., 68.
Belfast & M. L. R. Co. v. City of Belfast, 347, 348, 362, 365.
Bell v. Bank of Nashville, 36.
Belleville & I. R. Co. v. Gregory, 38, 47.
Bellows v. Bank, 81, 82.
 v. Hallowell, 557.
 v. Todd, 467, 491.
Bell's Appeal, 593.
Bell's Gap R. Co. v. Christy, 115.
Belmont v. Coleman, 599.
 v. Railway Co., 245.
Belo v. Commissioners, 223.
Belton, In re, 234-236.
Beman v. Rufford, 144.
Benbow v. Cook, 53, 142, 161.
Bend v. Bank Co., 411.
Bentlif v. Finance Corp., 636.
Bergman v. Association, 458, 459.
Berry v. Indemnity Co., 628.
Bertha Zinc & Mineral Co. v. Clute, 625.
Beveridge v. Railroad Co., 342, 343, 347.
Bickley v. Schlag, 380.
Bigelow v. Gregory, 58, 62, 94, 104, 110.
Bill v. Telegraph Co., 396, 397.
Binghamton Bridge, The, 126, 206.
Bird v. Hayden, 611.
Bird Coal & Iron Co. v. Humes, 506.
Bish v. Bradford, 288.
Bishop v. Brainerd, 78.
 v. Globe Co., 414.
Bissell v. Railroad Cos., 165, 172, 174, 180, 181, 184, 186, 529.
 v. Spring Valley Tp., 159.
Bissit v. Navigation Co., 559, 589, 592, 600.
Bjorngaard v. Bank, 477.
Black v. Canal Co., 126, 136, 144, 189, 204, 212.
 v. Huggins, 393, 394, 401.
 v. Zacharie, 417, 420, 424.
Blackburn Building Soc. v. Cunliffe, 179.
Black River Imp. Co. v. Holway, 102.
Black River & N. R. Co. v. Clarke, 315.
Black River & U. R. Co. v. Clarke, 100, 315, 316.
Blackstone Manuf'g Co. v. Inhabitants of Blackstone, 614, 617, 636.
Black & White Smiths' Society v. Vandyke, 405.
Blair v. Compton, 259, 260.
Blake v. Brown, 298.
 v. People, 38.
Blanchard v. Kaull, 13, 109.
Blanchards' Gun-Stock Turning Factory v. Warner, 129.
Bligh v. Brent, 258.
Bliss v. Irrigation Co., 161, 488.
Blodgett v. Morrill, 289, 305, 312.
Blouin v. Hart, 420.
Blunt v. Walker, 132.
Boardman v. Cutter, 259.
 v. Railway Co., 348, 349, 353, 366.
Board of Com'rs of City of St. Louis v. Shields, 107.
Board of Com'rs of Hamilton Co. v. Mighels, 32.
Board of Com'rs of Tippecanoe Co. v. Reynolds, 536.
Board of Directors v. Houston, 30.
Board of Education v. Bakewell, 29, 30.
 v. Greenebaum, 29, 30, 158.
Board of Revenue of Montgomery Co. v. Montgomery Gaslight Co., 223.
Board of Sup'rs v. People, 39.
Board of Trustees for Vincennes University v. State, 30.

[The figures refer to pages.]

- Board of Trustees of Illinois & M.
Canal v. Chicago & R. I. R. Co., 212.
Bocock's Ex'r v. Iron Co., 498.
Bogardus v. Trinity Church, 129.
Bommer v. Manufacturing Co., 114.
Bonaparte v. Railroad Co., 30, 53.
Bon Aqua Imp. Co. v. Standard Fire
Ins. Co., 83, 100.
Bond v. Appleton, 579.
Bone v. Canal Co., 168.
Bonnell v. Griswold, 610.
Booske v. Ice Co., 101.
Booth v. Bunce, 550.
v. Robinson, 142, 145, 393, 394.
v. Wonderly, 96.
Bosshardt & Wilson Co. v. Crescent Oil
Co., 140, 141, 185.
Boston Acid Manuf'g Co. v. Moring, 61.
Boston Barre & G. R. Co. v. Well-
ington, 310.
Boston Beer Co. v. Massachusetts, 208,
209, 211.
Boston Glass Manufactory v. Langdon,
234-237, 243, 249.
Boston Music-Hall Ass'n v. Cory, 417,
426.
Boston Water-Power Co. v. Boston &
W. R. Corp., 212.
Boston & A. R. Co. v. Pearson, 23.
v. Richardson, 429, 438.
Boston & Sandwich Glass Co. v. City
of Boston, 223.
Bostwick v. Chapman, 480.
Houlton Carbon Co. v. Mills, 381, 603.
Bouton v. Dement, 330.
Bow v. Allenstown, 36, 50.
Bowden v. Johnson, 582.
Boyce v. Coal Co., 174, 399.
v. Trustees, 106.
Boyd v. Railway Co., 300, 315, 316.
v. Worsted Mills, 350.
Boyer v. Boyer, 227.
Boykin v. State, 48.
Boynton v. Andrews, 381.
v. Hatch, 381.
Bradbury v. Canoe Club, 145, 147.
Bradford v. Railroad Co., 102.
Bradley v. Ballard, 181, 182, 185.
v. Bauder, 223, 224.
v. Case, 30.
v. Poole, 284.
v. Reppell, 89, 232.
Bradt v. Benedict, 236, 237.
Brady v. Moulton, 46.
Braintree Water-Supply Co. v. Town of
Braintree, 61.
Branch v. Jesup, 365.
v. Roberts, 608.
Brand v. Railroad Co., 297, 309, 312.
Brandenstein v. Hoke, 92, 106.
Branin v. Railroad Co., 211.
Brant v. Ehlen, 379, 380, 388, 389.
Brassey v. Railroad Co., 592.
Bray v. Farwell, 22, 24, 300.
Bretlung v. Lindauer, 611.
Brent v. Bank, 414.
Brewer v. Boston Theatre, 393, 394.
Brewster v. Hartley, 455, 458.
Brickerhoff v. Bostwick, 393, 401, 520.
Brickley v. Edwards, 101.
Brick Presbyterian Church v. Mayor,
etc., of New York, 209.
Briggs v. Penniman, 236, 540, 559, 567,
572, 588, 592, 597.
v. Spaulding, 505, 516, 517, 519, 607.
Brigham v. Mead, 317.
Bright v. Lord, 349.
Brinckerhoff v. Bostwick, 401, 516, 520,
607.
Brisbane v. Railroad Co., 349.
Bristol v. Sanford, 588.
British American Land Co. v. Ames,
634.
Broadway Bank v. McElrath, 425.
Broadwell v. Merritt, 101, 107.
Broderip v. Salomon, 56, 66.
Bronson v. Schneider, 572, 598, 602.
Brooklyn Steam Transit Co. v. City of
Brooklyn, 238.
Brooklyn, W. & N. Ry. Co. In re, 238.
Brown, In re, 356.
v. Adams, 420.
v. City of Atchison, 177.
v. Corbin, 70.
v. Hitchcock, 579.
v. Slate Co., 566.
v. Steamship Co., 490.
v. Winnisimmet Co., 142.
Bruce v. Platt, 609, 610.
Brum v. Insurance Co., 550.
Brundage v. Mining Co., 591-593.
Bryant v. Rich, 527.
B. S. Green Co. v. Blodgett, 137, 153.
Buchanan v. Meisser, 596.
Bucher v. Railroad Co., 282.
Buckeye Marble & Freestone Co. v.
Harvey, 151, 152, 172.
Budd v. Multnomah St. Ry. Co., 319,
320, 325, 326, 456, 458.
Buell v. Buckingham, 492, 511, 554.
Buffalo Lubricating Oil Co. v. Standard
Oil Co., 196.
Buffalo, N. Y. & E. R. Co., In re, 152.
Buffalo & A. R. Co. v. Cary, 88.
Buffalo & J. R. Co. v. Gifford, 265, 280,
281, 333, 334.
Buffalo & N. Y. C. R. Co. v. Dudley,
265, 267, 271, 313, 319, 321, 332, 458.
Buffalo & P. R. Co. v. Hatch, 59.
Buffett v. Railroad Co., 529.
Burlington v. Bardon, 113, 114.
Building & Loan Ass'n of Dakota v.
Chamberlain, 100, 101, 105, 107.
Bulkley v. Fishing Co., 159.
v. Whitcomb, 604.
Bullard v. Bank, 414, 459.
Bullock v. Railroad Co., 274.
v. Turnpike Co., 265, 278.
Buncombe Turnpike Co. v. McCaeson,
81.
Bundy v. Iron Co., 8.
Burbank v. Dennis, 117.
Burden v. Burden, 114, 455.
Burgess v. Seligman, 585.
Burke v. Badlam, 223.
v. Smith, 299, 305, 561, 592.

[The figures refer to pages.]

- Chestnut Hill & S. H. Turnpike Co. v. Rutter, 193, 195.
 Chew v. Bank, 435, 436.
 Chewacla Lime Works v. Dismukes, 135, 141, 172.
 Chicago, B. & Q. R. Co. v. Iowa, 211.
 Chicago City Ry. Co. v. Allerton, 54, 359, 303.
 Chicago Fair Grounds Ass'n v. People, 247.
 Chicago Gaslight & Coke Co. v. People's Gaslight & Coke Co., 144.
 Chicago, K. & W. R. Co. v. Stafford Co. Com'rs, 88.
 Chicago Life Ins. Co. v. Auditor of Public Accounts, 207, 211.
 v. Needles, 208, 210.
 Chicago, P. & S. W. R. Co. v. Town of Marseilles, 154.
 Chicago, R. I. & P. R. Co. v. Howard, 149.
 Chicago & A. Ry. Co. v. Derkes, 181.
 v. People, 210.
 Chicago & E. I. R. Co. v. People, 199.
 Chicago & E. R. Co. v. Flexman, 527.
 Chicago & N. W. R. Co. v. Auditor, 78.
 Child v. Coffin, 210.
 v. Hudson's Bay Co., 458.
 v. Iron Works, 573.
 Childs v. Bank, 195.
 v. Hurd, 58, 89.
 Chouteau Ins. Co. v. Floyd, 289, 330.
 Chouteau Spring Co. v. Harris, 407, 408, 412, 422, 427, 457, 582.
 Christensen v. Eno, 256, 370, 371, 378.
 Christian v. Mortgage Co., 625.
 Christian Church of Wolcott v. Johnson, 158.
 Chubb v. Upton, 100, 101.
 Church v. Coke Co., 157.
 Cicotte v. Catholic Church, 158.
 Cincinnati Mut. Health Assur. Co. v. Rosenthal, 626, 627, 629.
 Citizens' Mut. Fire Ins. Co. v. Sortwell, 471, 472.
 Citizens' Nat. Bank v. Elliott, 532.
 Citizens' State Bank v. Hawkins, 581.
 Citizens' & Miners' Sav. Bank & Trust Co. v. Gillespie, 591, 593.
 City Bank v. Bruce, 154.
 City Bank of Macon v. Bartlett, 239, 290.
 City of Atlanta v. Gate City Gaslight Co., 51.
 City of Chicago v. Cameron, 393, 395.
 v. Turner, 31.
 City of Corpus Christi v. Central Wharf & Warehouse Co., 181.
 City of Covington v. Covington & Cincinnati Bridge Co., 364.
 City of Davenport v. Dows, 393.
 City of Detroit v. Dean, 395.
 v. Detroit & H. P. R. Co., 216.
 City of Fall River v. County Com'rs of Bristol, 223.
 City of Lexington v. Butler, 146.
 City of Memphis v. Ensley, 223.
 v. Kimbrough, 31.
 City of Ottawa v. People, 38.
 City of Parkersburg v. Brown, 221.
 City of Roxbury v. Boston & P. R. Co., 217.
 City of Selma v. Mullen, 158.
 City Water Co. v. State, 143.
 City & County of San Francisco v. Spring Valley Waterworks, 45, 46, 47.
 Clapp v. Peterson, 155.
 Clark v. Bever, 376.
 v. Edgar, 530.
 v. Improvement Co., 263.
 v. Insurance Co., 462.
 v. Jones, 102.
 v. Navigation Co., 450, 451.
 Clarke v. Lumber Co., 336.
 Clarkson v. Clarkson, 357.
 Clayton v. Knob Co., 380.
 Clearwater v. Meredith, 136, 449.
 Clegg v. Grange Co., 57, 59.
 v. Hamilton & Wright County Grange Co., 110.
 Clem v. Railroad Co., 287.
 Cleveland v. Burnham, 580, 596.
 Cleveland Rolling-Mill Co. v. Texas & St. L. Ry. Co., 388, 592.
 Cleveland & M. R. Co. v. Robbins, 350.
 Close v. Glenwood Cemetery, 101, 107, 215.
 Clow v. Brown, 330.
 Clowe v. Product Co., 160.
 Coates v. Mayor, etc., of New York, 209.
 Coats v. Donnell, 554.
 Cobb v. Fant, 355.
 Cochran v. Arnold, 88, 91, 102, 104, 105, 109.
 v. Wiechers, 570, 587.
 Cockburn v. Bank, 336.
 Coe v. Railroad Co., 144, 378.
 Coffin v. Collins, 84, 85.
 v. Ransdell, 379, 380.
 v. Rich, 575.
 Cogswell v. Bull, 393, 394.
 v. Cogswell, 355.
 Colt v. Amalgamating Co., 330, 383.
 v. North Carolina Gold Amalgamating Co., 383.
 Colchester v. Seaber, 237.
 Cole v. Cassidy, 531.
 v. Millerton Iron Co., 540, 542.
 Coleman v. Coleman, 110.
 v. Railway Co., 135, 136.
 v. White, 567, 596, 602.
 Coles v. Kennedy, 286.
 Colfax Hotel Co. v. Lyon, 278.
 Colman v. Railway Co., 121.
 Colonial Bank v. Cady, 431, 432.
 Colorado Iron Works v. Sierra Grande Min. Co., 625, 635.
 Colt v. Ives, 420, 426, 427.
 Columbia Electric Co. v. Dixon, 100, 101, 103, 287, 317.
 Columbus Ins. Co. v. Walsh, 627.
 Commercial Bank v. French, 74.
 v. Newport Manuf'g Co., 147.
 v. Pfeiffer, 101.
 Commercial Bank of New Orleans v. Newport Manuf'g Co., 145.

CASES CITED.

[The figures refer to

Commercial Nat. Bank v. Farmers' & Traders' Nat. Bank, 280.	Cottin
Commissioners on Inland Fisheries v. Holyoke Water-Power Co., 210, 215, 217.	Cotto
Com. v. Bringham, 479.	Count
v. Chesapeake & O. R. Co., 222.	Far
v. Cullen, 53, 54, 487.	224.
v. Dalzell, 474, 475.	Count
v. Detwiller, 455.	rene
v. Eastern R. Co., 209, 212, 213, 217.	Court
v. Erie & N. E. R. Co., 126.	Covin
v. Essex Co., 210, 215.	552
v. Hemingway, 275, 478.	Cowle
v. Iron Co., 337.	Coxe
v. Milton, 617.	Craft
v. Northern Electric Light & Power Co., 68.	Cragi
v. Pike Beneficial Soc., 404.	Cran
v. President, etc., of Swift Run Gap Turnpike Co., 198.	Crav
v. Proprietors of New Bedford Bridge, 199, 200.	Creas
v. Pulaski Co. Agricultural & Mechanical Ass'n, 199.	590
v. St. Patrick's Society, 403.	Creas
v. Smith, 143, 144, 146.	Cred
v. Society, 402, 403.	501
v. Standard Oil Co., 222, 625.	Croc
v. Union Fire & Marine Ins. Co., 243-245.	Crok
v. Wickersham, 470.	Cron
v. Woelper, 455.	Cross
v. Worcester, 456.	v
Comstock, In re, 626, 629.	Crov
Cone Export & Commission Co. v. Poole, 634.	Crut
Congress & Empire Spring Co. v. Knowlton, 385.	Crut
Conklin v. Bank, 459.	Culb
Connecticut & P. R. R. Co. v. Bailey, 288, 304, 305, 309, 313, 318, 321, 331.	Culv
v. Baxter, 297.	Cun
Conner, Ex parte, 39.	Cun
Conro v. Gray, 552.	Curr
v. Iron Co., 447.	Curr
Conservators of the River Tone v. Ash, 13, 14, 17, 49, 72.	Curr
Cook v. Brick Co., 618.	
v. Railroad Co., 553.	Cuy
v. Sherman, 506.	
Cooper Manuf'g Co. v. Ferguson, 618, 624.	Dal
Copeland v. Manufacturing Co., 493, 510.	Dal
Copley v. Machine Co., 196.	Dal
Coppage v. Hutton, 272, 279.	Dal
Coppin v. Railroad Co., 153, 154.	Dal
Corey v. Morrill, 57, 100, 107, 296.	Dal
v. Wadsworth, 609.	Dal
Cork & B. Ry. Co. v. Cazenove, 275.	Dal
Cork & Y. Ry. Co., In re, 145, 177, 178.	Dal
Cornell's Appeal, 301, 311, 560.	Dal
Corning v. McCullough, 567, 570, 572, 602.	Dal
Cottheal v. Brouwer, 339.	Dal

[The figures refer to pages.]

- Davis v. Mining Co., 844.
 v. Proprietors of the Second Univ. Meetinghouse, 362.
 v. Railroad Co., 135, 137, 172, 173, 177, 510.
 v. Stevens, 583.
 Davison v. Gillies, 846.
 Day v. Bank, 635.
 v. Buggy Co., 140, 141, 177, 181, 185.
 v. India Rubber Co., 77, 637.
 v. Stetson, 67.
 v. Telegraph Co., 641.
 Dayton v. Borst, 319, 591, 592.
 Dean v. Davis, 49, 50, 88.
 De Gendre v. Kent, 349, 355.
 Delano v. Cnsc, 516, 607.
 Delaware Bay & C. M. R. Co. v. Markley, 46.
 Delaware Division Canal Co. v. Com., 199.
 Delaware Railroad Tax, 221, 228.
 Demarest v. Flack, 53, 66, 620.
 Denike v. Cement Co., 245.
 Denny Hotel Co. of Seattle v. Schram, 25, 65, 66, 151, 309-312.
 Densmore v. Shepard, 574.
 Densmore Oil Co. v. Densmore, 119.
 Dent v. Tramways Co., 243, 366.
 Denton v. Livingston, 259.
 Denver Fire Ins. Co. v. McClelland, 181, 183, 185, 186.
 Denver & R. G. Ry. Co. v. Harris, 195, 197, 524, 530.
 De Pass' Case, 582.
 De Peyster v. Insurance Co., 345.
 Derrickson v. Smith, 611.
 De Ruigne's Case, 372.
 Desdouty, Ex parte, 482.
 Despatch Line of Packets v. Bellamy Manuf'g Co., 435, 492, 493, 500.
 Detroit v. Mutual Gaslight Co., 142.
 Detwiler v. Com., 479, 484.
 De Voss v. City of Richmond, 81.
 Dewey v. Railway Co., 181, 182.
 De Witt v. Hastings, 102.
 Dexter & Mason Plank-Road Co. v. Miller, 319.
 Diamond Match Co. v. Roeber, 634.
 Dickenson v. Chamber of Commerce, 402, 403.
 Dillingham v. Snow, 36.
 Dimpfell v. Railway Co., 398, 399.
 Directors, etc., of Ashbury Railway Carriage & Iron Co. v. Riche, 127, 135, 167, 172.
 Directors, etc., of Central Ry. Co. of Venezuela v. Kisch, 284-286, 288, 290.
 Distilling & Cattle Feeding Co. v. People, 71, 188, 240, 241.
 Diversey v. Smith, 569, 587.
 Dobson v. Simonton, 89, 232, 249.
 Dodge v. Woolsey, 227, 392, 393.
 Dodgson's Case, 285.
 Donnelly v. Cordage Co., 77, 637, 639.
 Donohoe v. Mining Co., 486.
 Dooley v. Cheshire Glass Co., 100.
 Doolittle v. Marsh, 573.
 Dorris v. Sweeney, 103, 281.
 Doud v. Railway Co., 394, 395.
 Douglass v. Insurance Co., 461.
 v. Ireland, 380-382.
 Douglass County Com'rs v. Bolles, 101.
 Downing v. Board, 30, 202, 208.
 v. Marshall, 131, 132.
 v. Road Co., 121, 127, 135, 137, 140, 155, 172, 173, 502.
 Dows v. Naper, 107.
 Doyle v. Continental Ins. Co., 619.
 v. Mizner, 57, 103.
 Driscoll v. Manufacturing Co., 407, 413, 420, 458, 461.
 Dublin & W. Ry. Co. v. Black, 275.
 Ducat v. City of Chicago, 25, 616, 617.
 Dudley v. Collier, 627.
 v. High-School, 396.
 v. Kentucky High School, 445.
 Duggan v. Investment Co., 88, 92, 95.
 Duke v. Markham, 464.
 v. Navigation Co., 420.
 v. Taylor, 92, 103, 110.
 Dummer v. Smedley, 377.
 Duncomb v. Railroad Co., 142.
 Dunn v. University, 50.
 Dunphy v. Association, 394, 395, 398-400.
 Dunston v. Coke Co., 157.
 Dupee v. Water-Power Co., 139, 142, 154.
 Du Pont v. Tilden, 388.
 Durfee v. Railroad Co., 396, 397, 445, 449, 452.
 Dutcher v. Bank, 588.
 Dutchess Cotton Manufactory v. Davis, 100.
 Dutchess & C. O. R. Co. v. Mabbett, 279, 282, 283.
 Dutch West India Co. v. Van Moses, 73.
 Dwelling-House Ins. Co. v. Wilder, 633.
 Dwinelle v. Railroad Co., 527.
- E**
- Eagle Ins. Co. v. Ohio, 208, 210.
 Eakright v. Railroad Co., 59, 61.
 Earp's Appeal, 355, 357.
 East Alabama Ry. Co. v. Doe, 539.
 East Anglian Rys. Co. v. Eastern Counties Ry. Co., 135, 136, 167, 172.
 East Birmingham Land Co. v. Dennis, 428, 429.
 East Boston Freight R. Co. v. Eastern R. Co., 143, 145.
 Eastern Counties Ry. Co. v. Broom, 194, 527, 528.
 Eastern Plank-Road Co. v. Vaughan, 57.
 Eastern R. Co. v. Boston & M. R. Co., 54, 212, 486.
 East London Waterworks Co. v. Bailey, 157.
 Eastman v. Meredith, 81.
 East Norway Lake Church v. Froislie, 68, 91, 97, 107.

[The figures refer to pages.]

East Tennessee & V. R. Co. v. Gammon, 267, 319.
Eaton v. Aspinwall, 88, 100, 105.
 v. Bank, 309.
 v. Walker, 38, 91-93, 95, 103, 106, 110.
Ebbett's Case, 275.
Edelhoff v. State, 85.
Edgerly v. Emerson, 490, 491, 493.
Edgerton Tobacco Manuf'g Co. v. Croft, 402.
Edinboro Academy v. Robinson, 265.
Edinburgh L. & N. Ry. Co. v. Hebblewhite, 321.
Edison General Electric Co. v. Canadian Pac. Nav. Co., 627.
Edwards v. Fairbanks, 169.
Ehle v. Bank, 350.
Ehrman v. Insurance Co., 628.
Eidman v. Bowman, 54, 359, 360, 487.
Eisfeld v. Kenworth, 62.
Election of Directors of Chenango County Mut. Ins. Co., In re, 469, 481, 482.
Election of Directors of Long Island R. Co., In re, 455, 456, 458, 482.
Election of Directors of Mohawk & H. R. Co., In re, 469.
Elgin Butter Co. v. Elgin Creamery Co., 72.
Elias, In re, 484.
Eliot v. Himrod, 110.
Elizabethtown Gas Light Co. v. Green, 96.
Ellerman v. Stockyards Co., 149, 156.
Ellis v. Marshall, 52, 213.
 v. Ward, 515, 520, 606.
Ellison v. Railroad Co., 287.
Elston v. Piggott, 615.
Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 381, 387.
Emerson v. Machine Co., 634, 635.
Emery v. Parrott, 117, 118.
Emma Silver Min. Co. v. Grant, 117.
Empire City Bank, In re, 604.
Empire Mills v. Alston Grocery Co., 96, 105, 106, 110.
Empire Pass. Ry. Co., Appeal of, 337.
Empress Engineering Co., In re, 113.
Erie & N. E. Railroad v. Casey, 219.
Erlanger v. Phosphate Co., 118.
Essex Turnpike Corp. v. Collins, 293.
Estabrook, Ex parte, 147, 148, 176.
Estey Manuf'g Co. v. Runnels, 103, 106.
Eureka Iron & Steel Works v. Bresnahan, 142.
Evans v. Heating Co., 142, 465.
 v. Job, 47.
 v. Philadelphia Club, 402.
Evenson v. Ellingson, 92.
Everhart v. Railroad Co., 411, 450.
Excelsior Petroleum Co. v. Lacey, 353, 515, 607.
Excelsior Water & Mining Co. v. Pierce, 344, 346.
Ex-Mission Land & Water Co. v. Flash, 118, 119.
Exposition Ry. & Imp. Co. v. Canal St. E. Ry. Co., 809.

F

Fairbank v. Bank, 350.
Fairfield County Turnpike Co. v. Thorp, 7, 301.
Falconer v. Campbell, 37, 52.
Fanning v. Insurance Co., 268, 277.
Fargo v. Michigan, 226.
Farmers' Citizens' Bank v. Payne, 502, 503.
Farmers' Co-op. Trust Co. v. Floyd, 522.
Farmers' Loan & Trust Co. v. Toledo, A. A. & N. M. Ry. Co., 100.
Farmers' & Mechanics' Bank v. Baldwin, 128, 141, 170.
 v. Colby, 522.
Farmers' & Mechanics' Nat. Bank v. Dearing, 226.
Farmers' & Merchants' Bank v. Downey, 506.
 v. Wasson, 407, 409, 413.
Farmers' & Merchants' Bank of Lineville v. Wasson, 457.
Farmers' & Merchants' Ins. Co. v. Harrah, 626.
Farnsworth v. Wood, 588.
Farnum v. Ballard Vale Machine Shop, 599.
Farrar v. Walker, 289, 290.
Farrell Foundry v. Dart, 502, 503.
Farrington v. Railroad Co., 438, 489, 526.
 v. Tennessee, 223, 227.
Farrior v. Security Co., 623.
Fawcett v. Charles, 402.
Fay v. Noble, 109, 110, 496.
Fayette Land Co. v. Louisville & N. R. Co., 130, 168.
Fear v. Bartlett, 284, 289.
Fehr v. Gasch, 559, 561, 591.
Felgate's Case, 285.
Ferguson v. Wilson, 505.
Fertilizing Co. v. Hyde Park, 209.
Field v. Field, 470.
Fifth Ave. Bank of New York v. Forty-Second St. & Grand St. Ferry R. Co., 196, 438, 524, 525.
Fifth Ward Sav. Bank v. First Nat. Bank, 145, 147, 496, 498.
Filli v. Railroad Co., 638.
Filon v. Brewing Co., 148, 490.
Finn v. Brown, 578.
Finnegan v. Noerenberg, 88, 91-95.
Fire Department of New York v. Kip, 53.
Firemen's Benevolent Ass'n v. Lounsbury, 38.
First Nat. Bank v. Almy, 109.
 v. Christopher, 490.
 v. Council Bluffs City Waterworks Co., 496.
 v. Davies, 58.
 v. E. T. Barnum Wire & Iron Works, 558.
 v. Greene, 601.
 v. Gustin Minerva Con. Min. Co., 370, 373, 381, 383, 384.
 v. Hingham Manuf'g Co., 584.

[The figures refer to pages.]

- First Nat. Bank v. Lanier**, 440.
 v. National Exch. Bank, 152, 154.
 v. Peavey, 592.
 v. Pierson, 141.
 v. Price, 611.
 v. Stewart, 154.
First Parish in Sudbury v. Stearns, 470.
Fisher v. Bank, 258, 420, 424.
 v. Bush, 409, 480.
 v. Manufacturing Co., 25.
Fisk v. Railroad Co., 371, 540, 552.
Fisher v. La Rue, 158, 159.
Fitchburg R. Co. v. Grand Junction R. & D. Co., 217.
Fitts v. Palmer, 629.
Fitzgerald v. Missouri Pac. Ry. Co., 78.
Fitzpatrick v. Publishing Co., 387.
 v. Rutter, 100, 103.
Flash v. Conn., 570, 575, 596, 598.
Fleckner v. Bank, 158.
Fleener v. State, 84.
Flinn v. Bagley, 375.
Flint v. Pierce, 454, 460.
Flint & Fentonville Plank-Road Co. v. Woodhull, 218.
Flint & P. M. Ry. Co. v. Dewey, 506, 510.
Fogg v. Blair, 376.
Folger v. Insurance Co., 232, 245, 246, 251.
Fonds v. Assurance Co., 638.
Foot v. Mining Co., 395.
Ford v. Hill, 158.
 v. Thread Co., 343.
Foreman v. Bigelow, 411.
Forrest v. Manchester S. & L. Ry. Co., 400.
Ft. Edward & F. M. Plank-Road Co. v. Payne, 297.
Ft. Worth City Co. v. Smith Bridge Co., 138.
Foadlek v. Schall, 145, 592.
Foss v. Harbottle, 119, 392, 394, 396, 397.
Foster v. Bank, 251.
 v. Commissioners of Inland Revenue, 8.
 v. Essex Bank, 81.
 v. Moulton, 96.
 v. Planing-Mill Co., 554.
 v. Potter, 259, 260.
 v. White, 337, 339.
Fongeray v. Cord, 347, 353.
Fourth Nat. Bank v. Franchlyn, 575, 594, 595.
Fowler v. Bell, 158.
Fox v. Horah, 250, 252.
Franco-Texan Land Co. v. Laigle, 467.
Frankfort & S. T. Co. v. Churchill, 114.
Franklin Bank v. Commercial Bank, 151, 152.
Franklin Bridge Co. v. Wood, 41.
Franklin Co. v. Lewiston Inst. for Savings, 135, 141, 151, 171.
Franklin Fire Ins. Co. v. Hart, 58, 113.
 v. Jenkins, 519.
Franklin Glass Co. v. Alexander, 318.
Franklin Sav. Bank v. Bridges, 601.
Franks Oil Co. v. McCleary, 411.
Fredenburg v. Lyon Lake M. E. Church, 102.
Freeland v. Insurance Co., 100, 107.
Freeman v. Mill Co., 55.
French v. Teschemaker, 569.
Frenkel v. Hudson, 504.
Fresno Canal & Irr. Co. v. Warner, 101, 107.
Frost v. Walker, 23.
Frostburg Min. Co. v. Cumberland & P. R. Co., 81, 82.
Frye v. Partridge, 47.
Fulgum v. Railroad Co., 317.
Fuller v. Ledden, 572, 596.
Fuller & J. Manufg Co. v. Foster, 625.
Fusz v. Spannhorst, 606.
- G**
- Gable v. Miller**, 28.
Gaff v. Flesher, 411.
Galena & C. U. R. Co. v. Loomis, 208, 209.
Gallagher v. Brewing Co., 9.
Gallery v. National Exch. Bank, 510.
Galveston, H. & H. R. Co. v. Cowdrey, 145, 146.
Gamble v. Water Co., 380, 382, 387, 447, 477.
Gardner v. Insurance Co., 217, 254.
Garnett v. Richardson, 58, 110.
Garrett v. Mining Co., 381, 385.
 v. Plow Co., 611.
Garrison v. Howe, 568, 596, 597, 604, 610.
Gartside Coal Co. v. Maxwell, 109.
Gashwiler v. Willis, 447, 490.
Gaskill v. Dudley, 32.
Gauch v. Harrison, 604.
Gaus v. Switzer, 609, 610.
Gaylord v. Railroad Co., 552.
Geer v. School District, 8.
Gemmell v. Davis, 349-351.
Gent v. Insurance Co., 113.
Gentile v. State, 47.
Georg v. Railroad Co., 138.
German-American Inv. Co. v. City of Youngstown, 46.
Germania Ins. Co. v. Swigert, 622.
Germania Safety-Vault & Trust Co. v. Boynton, 148, 167.
Germantown Farmers' Mut. Ins. Co. v. Rhein, 175.
Germantown Pass. Ry. Co. v. Fittler, 320, 321, 559, 591, 593, 594.
Getty v. Devlin, 117, 118.
Gibbons v. Ellis, 311.
 v. Mahon, 356.
Gibbs v. Insurance Co., 635.
Gibson v. Furniture Co., 609.
 v. Moore, 234, 236.
Gifford v. Livingston, 14, 37.
Gilbert v. Hole, 168.
Gilbert's Case, 407, 408.
Gilchrist v. Railroad Co., 625.
Giles v. Hutt, 321.

[The figures refer

Gilkey v. Paine, 357.	G
Gill v. Balis, 330.	G
Gillespie v. Railroad Co., 52.	G
Gilman, C. & S. R. Co. v. Kelly, 510.	G
GIL	
Ginn v. Security Co., 623.	G
Girard v. Philadelphia, 74.	G
Glass v. Turnpike Co., 74.	G
Gleaves v. Turnpike Co., 53, 265, 267.	G
Glen Iron Works, In re, 373.	G
Glenn v. Howard, 324, 601.	G
v. Marbury, 601.	G
v. Orr, 84.	G
v. Semple, 601.	G
v. Williams, 601.	G
Globe Mut. Ben. Ass'n, In re, 65.	G
Gloninger v. Railroad Co., 145, 175.	G
Glover v. Lee, 554.	
Glymont Imp. & Exc. Co. v. Toler, 53, 55.	
Godbold v. Bank, 512.	G
Gogebic Inv. Co. v. Iron Chief Min. Co., 373.	G
Golden v. Morning News, 636.	G
Golden Gate Consolidated Hydraulic Min. Co. v. Superior Court, 200.	G
Goldsmith v. Insurance Co., 615.	G
Good Hope Co. v. Railway Barb Fencing Co., 636.	G
Goodin v. Canal Co., 510.	G
Goodrich v. Reynolds, 138, 141, 147, 288, 289.	Gr
Goodspeed v. Bank, 193, 195, 196.	G
Goodwin v. Hardy, 343.	G
v. Screw Co., 157, 158, 483.	G
Goodyear Rubber Co. v. George D. Scott Co., 609.	G
Gorder v. Canning Co., 161, 511.	G
Gordon v. Association, 37.	G
v. Preston, 8, 142, 504.	G
Gordon's Ex'rs v. Railroad Co., 362, 365, 367.	G
Gorham Manuf'g Co. v. Watson, 77, 637, 639.	G
Gormully & Jeffrey Manuf'g Co. v. Pope Manuf'g Co., 25.	G
Gorrell v. Insurance Co., 182.	G
Goshen & M. T. Co. v. Hurlin, 321.	G
Goss & P. Manuf'g Co. v. People, 259, 260.	G
Gould v. Town of Oneonta, 327.	G
Governor v. Allen, 27, 32.	
Gover's Case, 118.	
Graff v. Railroad Co., 411.	
Graham v. Railroad Co., 384, 468, 549, 550.	
Granby Mining & Smelting Co. v. Richards, 41, 58, 62.	I
Grand Gulf Bank v. Archer, 25.	I
Grand Rapids Bridge Co. v. Prange, 89, 90, 232.	I
Grand Rapids Sav. Bank v. Warren, 570, 571, 575.	I
Grand River Bridge Co. v. Rollins, 115.	I
Grangers Business Ass'n v. Clark, 101.	
Grant v. Railroad Co., 380.	
v. Ross, 354.	

[The figures refer to pages.]

- Haley v. Reid, 259, 260.
 Hall v. Insurance Co., 411, 462.
 v. Klinck, 596.
 v. Railroad Co., 111.
 v. Road Co., 428, 438, 440.
 v. Turnpike Co., 148.
 Hallam v. Hotel Co., 511, 512.
 Halsey v. McLean, 575, 609, 611.
 v. Railway Co., 140.
 Hambleton v. Glenn, 327, 411.
 Hamilton v. Glenn, 411.
 v. Keith, 202.
 v. Railroad Co., 96, 100, 811.
 Hamilton Mut. Ins. Co. v. Hobart, 254.
 Hammock v. Trust Co., 145.
 Hammond v. Jethro, 52.
 v. Straus, 58, 62.
 Hamsher v. Hamsher, 168.
 Hand v. Coal Co., 158.
 Handley v. Stutz, 375, 376, 878, 880,
 384, 468, 471, 603.
 Handy v. Draper, 602.
 Hanover Junction & S. R. Co. v. Grubb,
 296.
 Hanson v. Donkersley, 571.
 v. Little Sisters of the Poor, 168.
 Hardon v. Newton, 245, 246, 392.
 Hardy v. Merriweather, 147.
 Harger v. McCullough, 571.
 Harpold v. Stobart, 579, 580.
 Harriman v. Baptist Church, 138.
 v. Southam, 106.
 Harris v. First Parish, 596.
 v. McGregor, 57.
 v. Runnels, 627.
 Harrison v. Railway Co., 370.
 Harrod v. Hamer, 62.
 Hartford Fire Ins. Co. v. Raymond, 615,
 620.
 Hartford & N. H. R. Co. v. Boorman,
 411.
 v. Crosswell, 331, 392, 449, 451.
 v. Kennedy, 262, 319, 321.
 Harvard College v. Amory, 356.
 Haskell v. Worthington, 309.
 Haslett's Ex'rs v. Wotherspoon, 52.
 Hasselman v. Mortgage Co., 87, 91.
 Hassinger v. Ammon, 101.
 Hastings v. Drew, 540, 542, 563, 592,
 599.
 Hatch v. Borroughs, 571.
 v. Dana, 559, 592-594.
 Hathorne v. Calef, 575.
 Haven v. Asylum, 455.
 Hawes v. City of Oakland, 393-395, 398.
 Hawkins v. Glenn, 601.
 v. Mining Co., 113.
 Hawley v. Upton, 373.
 Hayes v. Shoemaker, 581.
 Hays v. Bank, 84, 609.
 v. Coal Co., 142, 145.
 v. Com., 204, 217.
 Hayward v. Davidson, 168.
 Haywood v. Lumber Co., 509, 606.
 Hazard v. Durant, 393, 394.
 Hazlett v. Butler University, 44, 46.
 Hazeltine v. Railroad Co., 866.
 Hazen v. Bank, 202.
 Hazlehurst v. Railroad Co., 151, 363.
 Heacock v. Sherman, 573.
 Head v. Insurance Co., 159.
 v. University of Missouri, 30.
 Heard v. Eldredge, 346.
 v. Talbot, 237, 243.
 Heart v. Bank, 413.
 Henston v. Railroad Co., 88, 106, 327.
 Heath v. Railway Co., 515, 520.
 v. Smelting Co., 468.
 Heck v. McEwen, 41.
 Hecla Consolidated Gold Min. Co. v.
 O'Neill, 273.
 Hedge & Horn's Appeal, 22, 265.
 Hegeman v. Railroad Corp., 209.
 Helms Brewing Co. v. Flannery, 181.
 Heining v. Manufacturing Co., 53.
 Heintzelman v. Association, 493.
 Heironimus v. Sweeney, 145.
 Hemingway v. Hemingway, 338.
 Hencke v. Twomey, 570.
 Hendee v. Pinkerton, 142, 144.
 Henderson & N. R. Co. v. Leavell, 296,
 304.
 Henkle v. Manufacturing Co., 584.
 Henriques v. Dutch West India Co.,
 634.
 Henry v. Railroad Co., 305, 315, 366,
 592, 594.
 Hersey v. Tully, 113.
 v. Veazie, 394, 401, 520.
 Hibernia Ins. Co. v. St. Louis & New
 Orleans Transp. Co., 540, 550.
 Hichens v. Congreve, 117.
 Hickling v. Wilson, 100, 305, 373.
 Hightower v. Thornton, 250, 261, 321,
 540, 555, 559, 600.
 Hildyard v. South-Sea Co., 428, 438.
 Hill v. Beach, 96, 110, 620.
 v. City of Boston, 31.
 v. Mining Co., 342, 348, 350, 352,
 353.
 v. Newichawanick Co., 348, 349.
 v. Publishing Co., 439, 526.
 Hiller v. Railroad Co., 636.
 Hillier v. Insurance Co., 603.
 Hill Manuf'g Co. v. Boston & L. R.
 Corp., 139.
 Hillyer v. Mining Co., 490.
 Hinchman v. Lincoln, 259.
 Hite's Devisees v. Hite's Ex'r, 357.
 Hoadley v. County Com'rs, 22.
 Hoare's Case, 584.
 Hodges v. Screw Co., 245, 515, 516, 518,
 520.
 Hodgson v. Railroad Co., 468.
 Hoffman v. Banks, 626.
 Hoffman Steam Coal Co. v. Cumber-
 land Coal & Iron Co., 512.
 Hohorst, In re, 639.
 Holbrook v. Zinc Co., 433, 434, 440,
 441.
 Holder v. Railway Co., 532.
 Holladay v. Elliott, 276.
 Hollins v. Brierfield Coal & Iron Co.,
 545, 546, 551, 552, 554.
 Holloway v. Railroad Co., 108.
 Holman v. State, 58, 241.

[The figures refer to pages.]

Holmes, *Ex parte*, 154, 475.
 v. Gilliland, 62.
 v. Sherwood, 592-594.
 Holmes, Booth & Haydens *v. Holmes*,
 Booth & Atwood Manuf'g Co.,
 73.
 v. Willard, 137, 517.
 Holmes & Griggs Manuf'g Co. *v.*
 Holmes & Wessell Metal Co., 153,
 169, 181.
 Holt *v. Bennett*, 511.
 Holt's Case, 285.
 Holyoke Bank *v. Burnham*, 579, 580,
 582, 584.
 v. Goodman Paper Manuf'g Co.,
 599.
 Home Ins. Co. *v. Swigert*, 623.
 Home of the Friendless *v. Rouse*, 227.
 Home Stock Ins. Co. *v. Sherwood*, 100.
 Hooker *v. New Haven & N. Co.*, 195.
 Hopper *v. Sage*, 349.
 Hoppin *v. Buffum*, 474, 475.
 Horn *v. Ivy*, 157.
 v. Railway Co., 209.
 Horn Silver Min. Co. *v. Ryan*, 515, 516,
 518-520.
 Horton *v. Wilder*, 478, 484.
 Hospes *v. Northwestern Manuf'g & Car*
 Co., 374, 383, 542, 544-546.
 Hotchkiss *v. Quarry Co.*, 356.
 Hotel Co. *v. Wade*, 513.
 Hough *v. Land Co.*, 168.
 Howe *v. Deuel*, 245.
 v. Starkweather, 260.
 Howell *v. Railway Co.*, 640.
 Hoyle *v. Railroad Co.*, 507, 512, 513.
 Hoyt *v. Thompson's Ex'r*, 630.
 Hubbard *v. Investment Co.*, 512.
 v. Weare, 344.
 Huddersfield Canal Co. *v. Buckley*, 411.
 Hudson *v. Carman*, 85.
 v. Green Hill Seminary Corp, 88, 91,
 95.
 v. Weir, 259.
 Hudson Real-Estate Co. *v. Tower*, 267-
 270.
 Hughes *v. Manufacturing Co.*, 265, 287,
 309, 319, 321, 330, 449.
 Hughesdale Manuf'g Co. *v. Vanner*, 62.
 Humble *v. Mitchell*, 258, 259.
 Humboldt Driving Park Ass'n *v. Ste-*
 vens, 361.
 Humboldt Min. Co. *v. American Manu-*
 facturing, Mining & Milling Co., 148.
 Humphrey *v. Association*, 174, 177.
 Humphreys *v. McKissock*, 7.
 v. Mooney, 61, 91, 109.
 Hun *v. Cary*, 515, 516, 518, 607.
 Hunt *v. Gaslight Co.*, 144.
 Hunter *v. Roberts*, 347.
 Hurlbut *v. Marshall*, 483.
 Huron Printing & Binding Co. *v. Kit-*
 tleston, 503.
 Hurt *v. Salisbury*, 58, 62, 94.
 Hutchins *v. Mining Co.*, 573, 614.
 v. Smith, 301.
 Hutchinson *v. Railroad Co.*, 198, 195,
 529.

Huyler *v. Cattle Co.*, 836, 838.
 Hyam's Case, 583.
 Hyatt *v. Allen*, 342, 412.
 Hyde *v. Doe*, 62.
 v. Goodnow, 625.
 Hyman *v. Coleman*, 571, 602.

I

Illinois Cent. R. Co. *v. Irvin*, 229.
 v. People, 202, 211.
 Illinois G. T. R. Co. *v. Cook*, 48.
 Illinois River R. Co. *v. Zimmer*, 54, 815,
 332, 451.
 Illinois Watch Case Co. *v. Pearson*, 72.
 Independent Order of Mutual Aid *v.*
 Paine, 100.
 Indiana *v. American Exp. Co.*, 618.
 v. United States, 40.
 Indianapolis, C. & L. R. Co. *v. Jones*,
 556.
 Indianapolis F. & M. Co. *v. Herkimer*,
 58, 103.
 Indianapolis & St. L. R. Co. *v. Vance*,
 221.
 Ingwersen *v. Edgecombe*, 609.
 Inhabitants of First Parish in Bruns-
 wick *v. Dunning*, 27.
 Inhabitants of First Parish in Sudbury
 v. Stearns, 482.
 Inhabitants of Fourth School Dist. *v.*
 Wood, 32.
 Instone *v. Frankfort Bridge Co.*, 265,
 267, 319, 321, 322.
 Insurance Co. *v. Morse*, 619.
 International Fair & Exp. Ass'n *v.*
 Walker, 267, 309, 311.
 Inverarity *v. Bank*, 504.
 Iowa Lumber Co. *v. Foster*, 151.
 Ireland *v. Reduction Co.*, 459.
 Irons *v. Bank*, 552, 580, 583.
 Irvin *v. Turnpike Co.*, 450.
 Isham *v. Buckingham*, 411, 420, 421.
 Isle Royale Land Corp. *v. Secretary of*
 State, 619.

J

Jackson *v. Brown*, 142.
 v. Meek, 579.
 v. Phillips, 248.
 v. Traer, 376.
 v. Walsh, 53, 54, 213, 218.
 Jackson's Adm'rs *v. Plank-Road Co.*,
 347, 352.
 Jacksonville, M. P. Ry. & Nav. Co. *v.*
 Hooper, 161.
 Jacobson *v. Allen*, 588.
 Jacobs Pharmacy Co. *v. Southern*
 Banking & Trust Co., 176.
 Jagger Iron Co. *v. Walker*, 571, 602.
 James *v. Woodruff*, 416.
 Jameson *v. People*, 36, 48.
 Jansen *v. Ostrander*, 27.
 Jarvis *v. Rogers*, 431.
 Jefferson Branch Bank *v. Skelly*, 227.

[The figures refer to pages.]

Jeffersonville, M. & I. R. Co. v. Beckwith, 558.
 Jefferys v. Gurr, 158.
 Jeffs v. York, 522.
 Jemison v. Bank, 210.
 Jenkins v. President, etc., 315.
 Jermain v. Railway Co., 349, 366, 412.
 Jessup v. Bridge, 142.
 v. Carnegie, 109.
 John v. Bank, 101, 237, 243.
 Johnson v. Bleaching Co., 579, 580.
 v. Corser, 95, 110.
 v. Fischer, 596.
 v. Kessler, 58.
 v. Laffin, 407, 408, 420, 457, 580-582.
 v. People, 38.
 v. Railroad Co., 47, 303, 304.
 v. Underhill, 580.
 v. Wabash & Mt. Vernon Plank-Road Co., 272.
 Johnston v. Gumbel, 102.
 v. Jones, 534.
 v. Shortridge, 504.
 Jones v. Avery, 573.
 v. Barlow, 611.
 v. Davis, 224.
 v. Foundry Co., 101, 103.
 v. Habersham, 168.
 v. Hardware Co., 91, 106.
 v. Herald Co., 237.
 v. Indemnity Co., 142.
 v. Jarman, 596.
 v. Morrison, 361, 510, 512, 532, 533.
 v. Railroad Co., 348, 352, 412.
 v. Sisson, 327.
 v. Smith, 626.
 v. Turnpike Co., 466, 471.
 Joslyn v. Distilling Co., 434, 440, 442.
 Junction R. Co. v. Reeve, 490.

K

Kadish v. Association, 180.
 Kaiser v. Bank, 57, 94, 110.
 Kanawha Coal Co. v. Coal Co., 49.
 Kansas Home Ins. Co. v. Wilder, 633.
 Kansas Pac. Ry. Co. v. Atchison, T. & S. F. R. Co., 40.
 Katama Land Co. v. Jernegan, 282, 318.
 Kaufman v. Wcolen Mills Co., 349.
 Kearsbey & Mattison Co., In re, 77, 637-639.
 Keating v. Stock Co., 260.
 Keeney v. Converse, 506, 513.
 Keller v. Johnson, 288, 301.
 Kelner v. Baxter, 113.
 Kelsey v. Fermentation Co., 339.
 Kendall v. Bishop, 553.
 Kennebec Co. v. Augusta Ins. & Banking Co., 614.
 Kenosha, R. & R. I. R. Co. v. Marsh, 449.
 Kent v. Mining Co., 362-364, 456, 459, 462.
 Kenton Furnace Railroad & Manufg Co. v. McAlpin, 370, 371.

Kernochan, In re, 349, 355-357.
 Keyser v. Hiltz, 276, 578, 586.
 Kidwelly Canal Co. v. Raby, 270.
 Kilgore v. Smith, 628.
 Kincaid v. Dwinelle, 569.
 Kindel v. Lithographing Co., 610, 627.
 King v. Amery, 237.
 v. Follett, 355.
 v. Governor, etc., of Bank of England, 363.
 v. Pasmore, 234.
 v. Railroad Co., 343, 351.
 Kirkland v. Kille, 610.
 Kirkpatrick v. United Presbyterian Church of Keota, 102.
 Klaus, Petition of, In re, 441, 457.
 Knight v. Barber, 259.
 Knott v. Insurance Co., 638.
 Knowles v. Board of Education, 47.
 v. Sandercock, 151.
 Knowlton v. Ackley, 594.
 v. Spring Co., 385.
 Knox v. American Co., 527.
 v. Baldwin, 610, 611.
 v. Eden Musee American Co., 429.
 Koehler v. Iron Co., 161, 505, 506.
 Kolff v. St. Paul Fuel Exchange, 468, 469.
 Koons v. Martin, 605.
 Kortright v. Bank, 441.
 Krulevits v. Railroad Co., 195, 196.
 Kruts v. Town Co., 89, 232, 249.
 Kunkelman v. Rentschler, 604.

L

Lackawanna Iron & Coal Co. v. Lezerne Co., 224.
 Ladd v. Cartwright, 591.
 Ladywell Min. Co. v. Brookes, 119.
 Lafayette, B. & M. Ry. Co. v. Cheeney, 532.
 Lafayette Ins. Co. v. French, 76, 635, 636.
 La France Fire-Engine Co. v. Town of Mt. Vernon, 627, 629.
 La Grange & M. R. Co. v. Rainey, 232.
 Lagrove v. Timmerman, 152.
 Laing v. Burley, 423.
 Lake Ontario, A. & N. Y. R. Co. v. Mason, 58, 272, 281, 324, 327, 601.
 Lake Ontario Shore R. Co. v. Curtiss, 274.
 Lake Shore & M. S. Ry. Co. v. Prentice, 195, 197.
 Lake Superior Iron Co. v. Drexel, 380, 381.
 Lamb v. Bowser, 625.
 v. Lamb, 623.
 Lamming v. Galusha, 83.
 Lamphere v. Lodge, 441.
 Lancaster v. Improvement Co., 66, 88, 614, 620, 632.
 Land Grant Railway & Trust Co. v. Board Co. Com'rs Coffey Co., 620, 622.
 Lane v. Brainerd, 304.
 Lane's Appeal, 593.

[The figures refer to

Larned v. Andrews, 627.	Logs
Lasher v. Stimson, 522.	177
Late Corporation of Church of Jesus Christ v. U. S., 252.	Long
Lathrop v. Bank, 129, 130, 158.	Long
Lauman v. Railroad Co., 64, 204.	Long
Lawrence v. Nelson, 608.	Long
Leavitt v. Mining Co., 488, 491, 492.	49
v. Palmer, 189.	Lore
Leazure v. Hillegas, 168.	Lore
Le Blanc, In re, 343, 563.	Lori
Lee & Co.'s Bank, In re, 216.	Lori
Legendre v. Association, 336.	Lori
Leggett v. Banking Co., 142, 161, 496, 497, 500.	Lori
Lehigh Bridge Co. v. Lehigh Coal & Nav. Co., 234.	Lori
Lehigh Coal & Nav. Co. v. Northampton Co., 229.	Lori
Lehman v. Warner, 101.	Lori
Lehman, Durr & Co. v. Glenn, 601.	Lori
v. Warner, 107.	Lori
Leipold v. Marony, 641.	Lori
Leitch v. Wells, 433.	Lori
Leland v. Hayden, 357.	Lori
Leloup v. Port of Mobile, 618.	Lori
Leo v. Railway Co., 142.	Lori
Le Roy v. Insurance Co., 343, 352, 563.	Lori
Leshner v. Karshner, 297.	Lori
Lester v. Bank, 190.	Lori
v. Webb, 499.	Lori
Levy Court v. Coroner, 32.	Lori
Lewey's Island R. Co. v. Bolton, 312.	Lori
Lewis v. Brainerd, 337.	Lori
v. Mill Co., 268.	Lori
v. Tilton, 522.	Lori
Lexington Life, Fire & Marine Ins. Co. v. Page, 8, 345, 504.	Lori
Lexington & O. R. Co. v. Bridges, 353, 515, 607.	Lori
Lexington & W. C. R. Co. v. Chandler, 327.	Lori
Libby v. Tobey, 381, 388.	Lori
Liebke v. Knapp, 379.	Lori
Life & Fire Ins. Co. v. Mechanic Fire Ins. Co., 128, 165, 166.	Lori
Lincoln Building & Sav. Ass'n v. Graham, 105.	Lori
Lincoln Shoe Manuf'g Co. v. Sheldon, 125.	Lori
Liquidators of The Imperial Mercantile Credit Ass'n v. Coleman, 505.	Lori
Little v. O'Brien, 331.	Lori
Littledale, Ex parte, 408.	Lori
Little Rock & Ft. S. Ry. Co. v. Perry, 114, 115.	Lori
Littlewort v. Davis, 175.	Lori
Liverpool Ins. Co. v. Massachusetts, 14, 17-19, 21, 615, 616.	Lori
Lloyd v. Preston, 382.	Lori
Loan Association v. Topeka, 221.	Lori
Lockhart v. City of Troy, 38.	Lori
v. Van Alstyne, 342, 343, 352, 365, 366.	Lori
Lockwood v. Bank, 458.	Lori
Logan v. Association, 182.	Lori
v. Railroad Co., 44.	Lori

[The figures refer to pages.]

- McCutcheon v. Mers Capsule Co., 153.
 McDaniels v. Manufacturing Co., 162, 472, 475.
 McDonnell v. Insurance Co., 100, 567, 572, 575, 598, 602.
 McDougald v. Bellamy, 48.
 Macdougall v. Gardiner, 396, 398.
 McDowall v. Sheehan, 588.
 M'Dowell v. Bank, 458.
 McElhenny's Appeal, 117.
 McFadden v. Board, 460.
 McGary v. People, 74.
 McGraw's Estate, In re, 168.
 Machias Hotel Co. v. Coyle, 281.
 Machinists' Nat. Bank v. Field, 429, 437.
 McIntire v. Preston, 141, 147, 176.
 Mack v. Iron Co., 395, 476.
 Mack's Appeal, 301, 560, 600.
 McKay v. Beard, 53.
 McKim v. Glenn, 411, 585.
 v. Odom, 35.
 McLaughlin v. Railroad Co., 345, 446, 500.
 McLennan v. Hopkins, 94.
 McLeod v. Mortgage Co., 617.
 McLoud v. Selby, 32.
 McMahon v. Macy, 585, 599.
 McMillan v. Railroad Co., 296, 333.
 McNaughton v. McLean, 260.
 McNeil v. Boston Chamber of Commerce, 498.
 v. Tenth Nat. Bank, 417, 420, 431, 432.
 McQueen v. Manufacturing Co., 634.
 McTighe v. Macon Const. Co., 88, 92.
 Madison, Watertown & Milwaukee Plank-Road Co. v. Watertown & Portland Plank-Road Co., 148.
 Magee v. Improvement Co., 181, 182.
 Magruder v. Colston, 582, 584.
 Mahomet v. Quackenbush, 39.
 Mahony v. Bank of State, 49.
 Main v. Mills, 344, 345, 354, 564.
 Mallett v. Simpson, 168.
 Mallory v. Oil Works, 150, 151.
 Manchester & L. R. R. v. Concord R. R., 177, 181.
 Mandlebaum v. Mining Co., 420, 437.
 Manhattan Beach Co. v. Harned, 438, 526.
 Manhattan Life Ins. Co. v. Fields, 630.
 v. Forty-Second St. & G. St. Ferry R. Co., 526.
 Manistee, The, 628.
 Mann v. Pentz, 592.
 Mann's Case, 581.
 Manufacturers' Ins. Co. v. Loud, 223, 230.
 Manufacturing Co. v. Bradley, 572, 597.
 Manville v. Karst, 604.
 v. Mining Co., 177.
 Marbury v. Land Co., 149.
 March v. Railroad Co., 348, 349, 412.
 Marchand v. Association, 112.
 Marcy v. Clark, 582.
 Marine Bank v. Ogden, 150, 151.
 Mariot v. Mascot, 17, 72.
 Market St. Ry. Co. v. Hellman, 129, 152.
 Marlborough Manuf'g Co. v. Smith, 421.
 Marlow v. Pittfield, 178.
 Marseilles Extension R. Co., In re, 490.
 Marsh v. Burroughs, 373, 593.
 Marshall v. Bank, 85, 516, 518, 607.
 v. Express Co., 498.
 v. Railroad Co., 75.
 Marshall Foundry Co. v. Killian, 540.
 Marshall Nat. Bank v. O'Neal, 176.
 Marson v. Delther, 263, 313.
 Martin v. Deets, 58, 89, 95.
 v. Fewell, 110.
 Martino v. Insurance Co., 461.
 Marysville Electric Light & Power Co. v. Johnson, 265, 267.
 Mason v. Alexander, 579.
 v. Harris, 114, 393.
 v. Mining Co., 251.
 Masonic Temple Ass'n of Minneapolis v. Channell, 301, 309, 311.
 Massachusetts General Hospital v. State Mut. Life Assur. Co., 217.
 Massachusetts Iron Co. v. Hooper, 413.
 Mathez v. Neidig, 568, 597, 603, 604.
 Mathis v. Pridham, 386.
 Matson v. Alley, 494, 501.
 Matthews v. Albert, 585.
 v. Associated Press, 456, 459, 460.
 v. Patterson, 609, 610.
 Maund v. Canal Co., 193, 194.
 Mayer v. Child, 259.
 Mayor, etc., of City of Norwich v. Norfolk Ry. Co., 162.
 Mayor, etc., of New York v. New York & Staten Island Ferry Co., 200.
 Mayor, etc., of Worcester v. Norwich & W. R. Co., 217.
 Mead v. City of New Haven, 31.
 Mechanics' Bank v. Merchants' Bank, 458.
 v. Seton, 441.
 Mechanics' Foundry & Machine Co. v. Hall, 318.
 Mechanics' & Farmers' Bank v. Smith, 461.
 Mechanics' & Traders' Branch of State Bank v. Debolt, 202, 227.
 Mechanics' & Workingmen's Mut. Sav. Bank v. Meriden Ag. Co., 151.
 Medical Inst. v. Patterson, 35.
 Medill v. Collier, 109, 110.
 Medway Collar Manufactory v. Adams, 74.
 Meeker v. Iron Co., 446, 512, 513.
 Melhado v. Railway Co., 112, 113.
 Melvin v. Insurance Co., 306, 330.
 Memphis Grain & Elevator Co. v. Memphis & C. R. Co., 148.
 Memphis & C. R. Co. v. Gaines, 223.
 Memphis & L. R. R. Co. v. Dow, 142, 386.
 Menier v. Telegraph Works, 303.
 Mercantile Bank v. City of New York, 227.
 Merchants' Bank v. Bliss, 611.
 v. Central Bank, 497.
 v. Cook, 8.

CASES CITED

[The figures refer to

Merchants' Bank v. State Bank, 104,	Minn
497.	39,
Merchants' Bank of Canada v. Liv-	Mino
ston, 432.	Mino
Merchants' Bank of New Haven v.	Mino
Bliss, 602.	Miss
Merchants' Fund Ass'n, Appeal of, 355,	Cro
356.	Miss
Merchants' Nat. Bank v. Lovitt, 504.	38.
Merchants' Nat. Bank of Gardiner v.	Miss
Citizens' Gaslight Co., 496, 501.	Mite
Merchants' & Manufacturers' Bank v.	v
Stone, 105.	v
Merrick v. Governor Co., 61.	Mite
v. Van Santvoord, 614, 615, 632.	Mob
Merrills v. Manufacturing Co., 195, 197.	Mob
Merrimac Min. Co. v. Bagley, 411.	
Merriman v. Magiveny, 91, 105.	Moh
Mersey Docks & Harbour Board Trus-	Moh
tees v. Gibbs, 194, 195.	W
Messersmith v. Bank, 411.	Mor
Methodist Church v. Pickett, 91, 101.	27
v. Remington, 130.	Moi
Metropolitan Bank v. Godfrey, 630.	10
Meyer v. Blair, 305.	Moi
Miami Powder Co. v. Hotchkiss, 91, 95.	v.
Middlesex Turnpike Corp. v. Locke, 331,	Moi
449.	5
Millbank v. Railroad Co., 151.	Mo
Millford & Chillicothe Turnpike Co. v.	10
Brush, 277, 331, 450.	Mo
Miller v. Bradish, 344.	1
v. Coal Co., 233.	Mo
v. Ewer, 55, 466.	
v. Insurance Co., 54, 172, 582.	
v. Manufacturing Co., 77, 637.	
v. Mining Co., 638.	
v. Newburg Orrel Coal Co., 89.	Mc
v. Railroad Co., 144, 217, 297, 301.	7
v. Ratterman, 365-368, 474.	Mc
v. Road Co., 57, 317, 319.	Mc
v. State, 213.	
v. White, 599, 611.	Mc
Mills v. Buenos Ayres Co., 546.	
v. County of St. Clair, 126.	
v. Northern Railway of Buenos	M
Ayres Co., 547.	
v. Stewart, 321, 322, 587.	M
Millward-Cliff Cracker Co., Estate of.,	M
496, 500.	
Miner v. Ice Co., 246, 393, 446, 493, 509,	M
510, 533.	M
Mineral Point R. Co. v. Keep, 25, 538.	M
Miners' Bank v. U. S., 29.	M
Miners' Bank of Dubuque v. U. S., 218.	N
Miners' Ditch Co. v. Zellerbach, 142,	
172, 174.	
Mining Co. v. Anglo-Californian Bank,	M
487, 498.	
Minneapolis Threshing-Mach. Co. v. Da-	M
vis, 271, 307, 308.	
Minneapolis Times Co. v. Nimocks, 492.	
Minneapolis & St. L. Ry. Co. v. Bas-	
sett, 315.	
Minnehaha Driving Park Ass'n v. Legg,	
319.	
Minnesota Gaslight Economizer Co. v.	
Denslow, 101, 107.	

[The figures refer to pages.]

Mt. Holly Lumberton & Medford Turnpike Co. v. Fenece, 431.
 Mount Palatine Academy v. Kleinschnitz, 74.
 Mount Pleasant v. Beckwith, 556.
 Mt. Sterling Coal-Road Co. v. Little, 274.
 Mowbray v. Antrim, 515, 607.
 Mower v. Staples, 450.
 Mowrey v. Railroad Co., 449.
 Mozley v. Alston, 394.
 Mullanphy Sav. Bank v. Schott, 511.
 Muller v. Dows, 75, 76, 78.
 Mulrey v. Insurance Co., 462.
 Mumma v. Potomac Co., 206, 236, 249, 556.
 Muncy Traction Engine Co. v. De La Green, 268.
 Munn v. Commission Co., 138, 147.
 v. Illinois, 211.
 Munson v. Railway Co., 113, 510, 512.
 Murphy, Ex parte, 482.
 Muscatine Water Co. v. Muscatine Lumber Co., 158.
 Muskingum Valley Turnpike Co. v. Ward, 330.
 Mussina v. Goldthwaite, 520.
 Myers v. Manhattan Bank, 35, 36.
 Mylrea v. Railway Co., 235, 237, 241.

N

Naglee v. Wharf Co., 423.
 Narragansett Bank v. Atlantic Silk Co., 99, 147, 496.
 Nashua & L. R. Corp. v. Boston & L. R. Corp., 78, 177.
 Nassau Bank v. Jones, 151, 172, 185, 188.
 Nassau Gaslight Co. v. City of Brooklyn, 68.
 Nathan v. Tompkins, 393, 472, 534.
 v. Whitlock, 582.
 National Bank v. Case, 583, 584.
 v. City of Boston, 226, 227.
 v. Com., 230.
 v. Graham, 530.
 v. John G. Mattingly & Sons, 148.
 v. Matthews, 190.
 v. Texas Inv. Co., 58, 70.
 v. Watsonstown Bank, 414.
 v. Whitney, 190.
 v. Young, 148, 176.
 National Building Society, In re, 145, 146.
 National Button Works v. Wade, 639.
 National Commercial Bank v. McDonnell, 276, 292, 579, 584.
 National Loan & Building Ass'n v. Lichtenwalner, 571.
 National Mut. Fire Ins. Co. v. Pursell, 626, 629.
 National Park Bank v. German-American M. W. & S. Co., 147-149, 176.
 National Pemberton Bank v. Porter, 141, 170.
 National Permanent Benefit Building Soc., In re, 178, 179.

National Tube-Works Co. v. Ballou, 597.
 v. Gilfillan, 381.
 Natoma Water & Mining Co. v. Clarkin, 168.
 Natusch v. Irving, 448, 453.
 Neall v. Hill, 245, 516, 518, 534.
 Nelligan v. Campbell, 522.
 Nelms v. Mortgage Co., 617.
 Nelson v. Eaton, 145, 156.
 v. Hubbard, 386.
 v. Railroad Co., 209.
 Nenny v. Waddill, 385.
 Neuchatel Asphalt Co. v. Mayor, etc., 628.
 Neustadt v. Railroad Co., 227.
 Nevada Bank of San Francisco v. Portland Nat. Bank, 196.
 Nevitt v. Bank, 540, 559.
 New Albany & S. R. Co. v. Fields, 287.
 v. McCormick, 296, 317.
 v. Pickens, 823.
 Newberry v. Manufacturing Co., 423, 424.
 Newby v. Railway Co., 78.
 New Castle Northern R. Co. v. Simpson, 177, 385, 386.
 Newell v. Railway Co., 636.
 New England Mortg. Security Co. v. Ingram, 617.
 New Hampshire Central Railroad v. Johnson, 309.
 New Haven, M. & W. R. Co. v. Town of Chatham, 502.
 New Haven & D. R. Co. v. Chapman, 204, 217.
 New Jersey Railroad & Transp. Co. v. Hancock, 229.
 New Orleans v. Houston, 227, 230.
 New Orleans Gaslight Co. v. Louisiana Light & H. P. & Manuf'g Co., 36, 37, 205, 206.
 New Orleans, J. & G. N. R. Co. v. Harris, 143, 204.
 New Orleans Waterworks Co. v. Rivers, 37, 206.
 Newport & C. Bridge Co. v. Woolley, 78.
 Newton Manuf'g Co. v. White, 235.
 New York El. R. Co., In re, 41, 45.
 New York Exchange Co. v. De Wolff, 297, 312.
 New York Firemen Ins. Co. v. Ely, 138.
 New York, H. & N. R. Co. v. Hunt, 312.
 New York Institution for the Blind v. How's Ex'rs, 74.
 New York, L. E. & W. R. Co. v. Com., 615.
 v. Haring, 193, 194, 529.
 v. Nickals, 347, 366, 367.
 New York Protective Ass'n v. McGrath, 402.
 New York & G. L. R. Co. v. State, 198.
 New York & M. L. R. Co. v. Winans, 136, 144.
 New York & N. H. R. Co. v. Ketchum, 112, 532.
 v. Schuyler, 359, 360, 423, 437, 438, 440, 499, 525, 528.

[The figures refer to

New York & O. M. R. Co. v. Van Horn,	Ohio &
315.	
New York & S. Canal Co. v. Fulton	v.
Bank, 131, 151.	Olcott
Niagara County Bank v. Baker, 141.	Old Co
Nichols v. New Haven & Northampton	Oldtov
Co., 227, 228.	O'Lea
Nickalls v. Merry, 581.	Oler v
Nicoll v. Railroad Co., 129, 130, 140.	Oliver
Nims v. Mt. Hermon Boys' School, 194,	v.
195.	Olney
v. School, 527, 529.	O'Nen
Nockels v. Crosby, 112.	Oneld
Norfolk & W. R. Co. v. Pennsylvania,	Ooreg
616, 618.	Rop
Norris v. Staps, 454.	Openi
North v. Forest, 259.	205.
v. State, 87, 91.	Orego
North Chicago City Ry. Co. v. Gastka,	Nav
527.	Oregc
Northern Cent. Michigan R. Co. v. Es-	Co.,
low, 294.	O'Rel
Northern Cent. R. Co. v. Com., 199.	O'Rei
North Hudson Mut. Bldg. & Loan Ass'n	Orms
v. Childs, 505, 518.	Orov
North River Boom Co. v. Smith, 46.	Plu
Northrop v. Bushnell, 305, 373.	Orr v
v. Turnpike Co., 424.	v
North State Copper & Gold Min. Co. v.	v
Field, 639, 640.	Osbo
Northumberland Hotel Co., In re, 114.	v
Northwestern Fertilizing Co. v. Village	Osgo
of Hyde Park, 126.	Oska
Northwestern Mut. Life Ins. Co. v. Cot-	312
ton-Exchange Real-Estate Co.,	Otis
381.	Otto
v. Elliott, 625, 626.	Over
v. Overholt, 627.	Over
Northwestern Packet Co. v. Shaw, 140,	Se.
141, 172.	Orei
Northwestern Union Packet Co. v.	Owe
Shaw, 172, 177, 178.	v
Northwestern University v. People, 227,	Oxfo
229.	
Northwest Transp. Co. v. Beatty, 477.	
North & S. St. R. Co. v. Spullock, 324.	
Norton v. Shelby Co., 98.	Pac
Norwich Gaslight Co. v. Norwich City	Pac
Gas Co., 36, 37.	Pac
Norwood & B. Co. v. Andrews, 139.	
Nugent v. Supervisors, 332.	Pad
Nulton v. Clayton, 277.	30
Nute v. Insurance Co., 456.	Pag
Nutter v. Railroad Co., 809, 810.	
	Pai
	Pal
	Pal
O	
O'Donald v. Railroad Co., 301.	Pal
Ogden v. City of St. Joseph, 223, 224.	4
Ogilvie v. Insurance Co., 290, 373, 559,	Pai
592, 593.	Pai
Ohio Life Insurance & Trust Co. v.	Pai
Merchants' Insurance & Trust Co.,	Pai
258, 540.	Pai
Ohio & I. R. Co. v. Ridge, 84.	Pa.
Ohio & M. Ry. Co. v. McCarthy, 139.	
v. McClelland, 209.	

[The figures refer to pages.]

- Parker v. Railroad Co.**, 100, 218, 218, 294.
 v. Railway Co., 126.
 v. Thomas, 287, 288, 296, 301.
Parrot v. Lawrence, 126.
Parrott v. Colby, 571, 602.
Parson v. Joseph, 371.
Passenger R. Co. v. Young, 527.
Patent File Co., In re, 142, 145.
Patterson v. Lynde, 591, 592, 641.
 v. Manuf'g Co., 610.
 v. Robinson, 156.
Patty v. Mill Co., 269.
Paul v. City of Kenosha, 177.
 v. Commonwealth of Virginia, 76, 615-618.
Pauly v. Trust Co., 584.
Paxton Cattle Co. v. First Nat. Bank, 115, 116.
Payne v. Bullard, 830, 373, 559, 561, 592, 594, 600.
Payson v. Withers, 625.
Peabody v. Flint, 393, 400, 402.
 v. Speyers, 259.
Peake v. Railroad Co., 85.
Peace v. Railroad Co., 135, 136, 140, 172, 173.
Pearson v. Concord R. Corp., 151, 511, 512.
Peck v. City of San Antonio, 39.
Peckham v. Inhabitants, 634.
 v. Van Wagenen, 352.
Peirce v. Building Co., 464.
Pembina Con. Silver Mining & Milling Co. v. Pennsylvania, 618.
Pender v. Lushington, 474, 476.
Peninsular Ry. Co. v. Duncan, 279.
Penn Match Co. v. Hapgood, 113.
Pennsylvania R. Co. v. St. Louis, A. & T. H. R. Co., 80, 136.
Pennypacker v. Insurance Co., 628.
Penobscot Boom Corp. v. Lamson, 67.
Penobscot R. Co. v. Dummer, 265, 309, 313, 484.
 v. White, 294, 309, 312, 326.
Penobscot & K. R. Co. v. Bartlett, 310.
Pensacola Tel. Co. v. Western Union Tel. Co., 618.
People v. Albany & V. R. Co., 200.
 v. Assessors of Village of Watertown, 5, 6, 14.
 v. Batchelor, 465.
 v. Board, 88.
 v. Boston & A. R. Co., 210.
 v. Bowen, 47.
 v. Campbell, 139.
 v. Central Car & Manuf'g Co., 353.
 v. Chambers, 58, 63.
 v. Cheeseman, 57, 59.
 v. Chicago Gas Trust Co., 71, 240.
 v. Coleman, 22, 23.
 v. Commissioners of Taxes, etc., for the City & County of New York, 228, 256.
 v. Crockett, 441, 458.
 v. Crossley, 455, 479.
 v. Cummings, 464.
 v. England, 531.
People v. Equitable Trust Co. of New London, 617.
 v. Farnham, 48.
 v. Fire Ass'n of Philadelphia, 615, 623.
 v. Goss & Phillips Manuf'g Co., 260.
 v. Hamill, 89.
 v. Horn Silver Min. Co., 623.
 v. Hurlbut, 31.
 v. Kingston & M. Turnpike Road Co., 9, 48.
 v. Knickerbocker Ice Co., 69.
 v. Lake Shore & M. S. R. Co., 337.
 v. La Rue, 88, 129.
 v. Mahaney, 37.
 v. Marshall, 36.
 v. Mauran, 130.
 v. Maynard, 36.
 v. Montecito Water Co., 57, 63.
 v. Nelson, 69.
 v. North River Sugar-Refining Co., 9, 71, 239, 240.
 v. O'Brien, 215.
 v. Ottawa Hydraulic Co., 39.
 v. Parker Vein Coal Co., 640.
 v. Peck, 465, 469.
 v. Perrin, 48.
 v. Phillips, 482.
 v. Phoenix Bank, 242.
 v. River Raisin & L. E. R. Co., 138.
 v. Robinson, 421.
 v. San Francisco Sav. Union, 344.
 v. Selfridge, 57, 63.
 v. Steamship Co., 339.
 v. Stockton, 59.
 v. Throop, 336, 337.
 v. Township Board of Overysel, 509.
 v. Troy House Co., 69.
 v. Twaddell, 479.
 v. Utica Ins. Co., 25.
 v. Water Co., 59.
 v. Weaver, 227.
 v. Wemple, 68, 617, 618, 623.
 v. Young Men's Father Matthew T. A. B. Soc., 456, 457.
People's Bank v. Gridley, 420, 424.
People's Ferry Co. v. Balch, 297, 299, 309.
People's Mut. Ins. Co. v. Westcott, 325, 465.
Peoria & S. R. Co. v. Thompson, 386.
Perine v. Grand Lodge, 99.
Perkins v. Sanders, 51, 53.
 v. Savage, 292.
Perrin v. Granger, 319.
Perry v. Railway Co., 117.
 v. Turner, 596.
 v. Tuscaloosa Cotton Seed Oil Mill Co., 371, 472, 506, 515, 534.
Peterson v. City of New York, 158.
Pettis v. Atkins, 110.
Pfohl v. Simpson, 597.
Phelan v. Hazard, 390.
Phelps v. Bank, 342, 348, 349.
Phenix Ins. Co. v. Burdett, 615, 617, 620.

[The figures refer

Philadelphia Trust, Safe-Deposit & Ins. Co., Appeal of, 357.	Por
Philadelphia, W. & B. R. Co. v. Cowell, 352.	Por
v. Maryland, 228.	pi
v. Quigley, 193, 195, 524.	Por
v. Woelpper, 145.	Por
Philadelphia & R. R. Co. v. Fidelity Insurance, Trust & Safe-Deposit Co., 147.	Por
v. Smith, 146.	F
Philadelphia & Southern S. S. Co. v. Pennsylvania, 226.	Por
Philadelphia & S. R. Co. v. Lewis, 175.	3
Philadelphia & W. C. R. Co. v. Hickman, 296, 297, 309, 316.	Por
Phillips v. Bridge Co., 39, 311, 312.	Por
v. Town of Albany, 39.	Por
v. Wickham, 234, 479.	Por
Phinney v. Murray, 349.	Por
v. Railroad Co., 102.	2
Phipps v. Jones, 269.	Por
Phoenix Ins. Co. v. Welch, 615.	e
Phoenix Iron Co. v. Com., 337, 338.	Por
Phoenix Warehousing Co. v. Badger, 100, 323, 330, 333, 561.	Por
Pickard v. Car Co., 618.	Por
Pier v. Hanmore, 609, 610.	Por
Pierce v. Construction Co., 598.	Por
Pike v. Railroad Co., 326.	Por
Pinkerton v. Railroad Co., 426, 441.	Por
Pitcher v. Board of Trade, 403, 404.	4
Pittsburg, F. W. & C. R. Co. v. Com., 223.	Por
Pittsburg Min. Co. v. Spooner, 117, 118.	Por
Pittsburg & C. R. Co. v. Southwest P. Ry. Co., 210.	Por
Pittsburg & T. Copper Co. v. Quintrell, 114.	Por
Pittsburgh, C. & St. L. Ry. Co. v. Keokuk & H. Bridge Co., 173, 175.	Por
Pittsburgh & Allegheny Bridge Co. v. Com., 199.	Por
Pittsburgh & C. R. Co. v. Clarke, 411, 414.	Por
Pittsburgh & S. R. Co. v. Biggar, 300.	Por
Pixley v. Railroad Co., 157-159.	Por
Plank's Tavern Co. v. Burkhard, 269.	Por
Planters' Bank v. Sharp, 211.	Por
Planters' & Merchants' Bank v. Andrews, 25.	Por
Planters' & Merchants' Mut. Ins. Co. v. Selma Sav. Bank, 458.	Por
Planters' & Miners' Bank v. Padgett, 109.	Por
Plaquemines Tropical Fruit Co. v. Buck, 117.	Por
Platt v. Railroad Co., 592.	Por
Plimpton v. Bigelow, 260.	Por
Plymouth R. Co. v. Colwell, 538.	Por
Polk v. Plummer, 27, 32.	Por
Pollard v. Bailey, 596.	Por
Polleys v. Insurance Co., 7.	Por
Pollock v. Bank, 428, 429.	Por
Pond v. Railroad Co., 546, 548.	Por
Pooch v. Association, 182.	Por
Poole, Jackson & Whyte's Case, 609.	Por

[The figures refer to pages.]

Proprietors of Canal Bridge v. Gordon, 158.
 Proprietors of Charles River Bridge v. Proprietors of Warren Bridge, 204.
 Proprietors of City Hotel v. Dickinson, 58, 61.
 Proprietors of Jeffries Neck Pasture v. Inhabitants of Ipswich, 25.
 Proprietors of Union Locks & Canals v. Towne, 331, 449.
 Protection Life Ins. Co. v. Foote, 483.
 Providence Bank v. Billings, 127, 210, 221.
 Pugh and Sharman's Case, 276.
 Pulford v. Fire Department, 402.
 Pullman v. Upton, 411, 413.
 Pullman's Palace Car Co. v. Missouri Pac. Ry. Co., 556.
 Pumphrey v. Threadgill, 145.

Q

Queen, The, v. Arnaud, 6, 7.
 Queenan v. Palmer, 570, 596.
 Quick v. Lemon, 274.
 Quincy Railroad Bridge Co. v. Adams Co., 79, 80.
 Quinlan v. Railway Co., 53.

R

Racine & M. R. Co. v. Farmers' Loan & Trust Co., 78.
 Railroad v. Berks Co., 229.
 Railroad Co. v. Harris, 615, 635.
 v. Howard, 142.
 v. Peniston, 226.
 v. Richmond, 210.
 v. Smith, 367.
 Railroad Tax Cases, 225.
 Railway Co. v. Allerton, 487.
 v. Whitton's Adm'r, 78.
 Ramsey v. Manufacturing Co., 284.
 Rand v. Hubbell, 357.
 Ranzer v. Railway Co., 285.
 Rankine v. Elliott, 591, 592.
 Rathbone v. Gas Co., 394.
 Rathbone, Sard. & Co. v. Frost, 629.
 Rathbun v. Snow, 461, 495, 498-500.
 Ratterman v. Telegraph Co., 618.
 Read v. Frankfort Bank, 206.
 v. Gas Co., 309, 325, 326, 490.
 Rece v. Newport News & M. V. Co., 78.
 Receivers of Bank of Circleville v. Renick, 237.
 Reciprocity Bank, In re, 586.
 Rector, etc., of Christ Church v. County of Philadelphia, 228.
 Redington v. Coruwell, 605.
 Redmond v. Manufacturing Co., 640.
 Red Wing Hotel Co. v. Friedrich, 265, 303.
 Reed v. Bank, 196.
 v. Copeland, 420.
 v. Hend, 355.
 v. Railway Co., 57.

Reed v. Walker, 625.
 Reed Bros. Co. v. First Nat. Bank, 550.
 Reeves v. Harper, 625.
 Reg. v. Great North of England Ry. Co., 198, 199.
 v. Registrar, 72, 73.
 Regents v. Williams, 30.
 Regents of University of Maryland v. Williams, 30, 65, 219.
 Regents of University of Michigan v. Detroit Young Men's Soc., 129, 140, 156, 158, 160.
 Reichwald v. Hotel Co., 114, 142, 145, 236, 487, 500, 553, 554, 614.
 Reid v. Manufacturing Co., 345, 354, 459, 559, 564.
 Reiser v. Strong, 89.
 Reliance Mut. Ins. Co. v. Sawyer, 626.
 Remington v. Bay Co., 597.
 Rensselaer & Washington Plank-Road Co. v. Barton, 319.
 Republican Mountain Silver Mines v. Brown, 630, 640.
 Rex v. Amery, 52, 53.
 v. Gardner, 25.
 v. Governor, etc., of Bank of England, 353.
 v. Richardson, 402.
 v. Westwood, 52.
 Reynolds' Widow v. Commissioners, 142.
 Rhey v. Plank-Road Co., 274.
 Rice v. Rockefeller, 408, 441.
 Richards v. Insurance Co., 600.
 v. Railroad Co., 142.
 Richardson v. Buhl, 71.
 v. Railroad Co., 466, 471.
 v. Sibley, 143, 144.
 Richelieu Hotel Co. v. International Military Encampment Co., 137, 265, 270, 287.
 Richmond v. Irons, 570, 580, 585, 587, 602.
 Richmond Factory Ass'n v. Clarke, 103, 281, 282.
 Richmond, F. & P. R. Co. v. Sneed, 147.
 Richmond St. R. Co. v. Reed, 282.
 Rickart v. People, 22.
 Rickerson Roller-Mill Co. v. Farrell Foundry & Machine Co., 375, 383.
 Ricord v. Railroad Co., 139.
 Riddle v. Proprietors, 32, 195.
 Rider v. Fritchey, 573.
 Ridgefield & N. Y. R. Co. v. Brush, 312.
 Ridgway v. Bank, 176.
 Rikoff v. Machine Co., 103.
 Rising Sun Ins. Co. v. Slaughter, 626, 629.
 Rivanna Nav. Co. v. Dawsons, 129-130, 131.
 Rives v. Dudley, 130.
 Robbins v. Butler, 23.
 v. Taxing Dist., 618.
 Roberts v. Woodworking Co., 160.
 Roberts Manuf'g Co. v. Schlick, 113.
 Robertson v. Bullions, 28.
 Robinson v. Bank, 350.
 v. Lodge, 404.
 v. Railroad Co., 305.

CASES CITED.

[The figures refer to p

Robinson v. Smith, 392, 505, 515, 516, 520.	St. John
v. Turrentine, 276, 586.	St. Jose
Rockford, R. I. & St. L. R. Co. v. Sage, 112.	45, 53
v. Shunick, 284, 291.	St. Law
Rockland, Mt. D. & S. Steamboat Co. v. Sewall, 309.	St. Loui
Rock River Bank v. Sherwood, 175.	v. S
Rocky Mountain Nat. Bank v. Bliss, 598.	St. Loui
Rogers v. Land Co., 115.	v. T
v. Society, 8, 59.	St. Lou
Rogers, L. & M. Works v. Southern Railroad Ass'n, 149.	com,
Rollins v. Carriage Co., 554.	St. Lou
Roman Catholic Orphan Asylum v. Abrams, 59.	low,
Roosevelt Hospital v. Mayor, etc., of City of New York, 228.	St. Lou
Root v. Sinnock, 567, 579.	L. R.
Rorke v. Thomas, 353, 610.	St. Lou
Roseboom v. Whittaker, 511, 609.	Haut
Rose Hill & E. R. Co. v. People, 85.	St. Pau
Rosenthal v. Madison & I. P. Co., 44.	44.
Rosevelt v. Brown, 584.	St. Pa
Ross-Meehan, B. S. F. Co. v. Southern M. Iron Co., 126.	263,
Rothchild v. Hoge, 316.	Salem
Rounds v. Railroad Co., 527.	of D
Rouse v. Bank, 554.	Salem
Royal Bank of Liverpool v. Grand Junction Railroad & Depot Co., 161, 162.	292,
Rue v. Railway Co., 630.	Salmo
Ruggles v. People, 202, 211.	Salom
Rundle v. Delaware & R. Canal, 30.	Salt I
Runyan v. Coster's Lessee, 130, 631.	524,
Ruse v. Bromberg, 323, 324.	Saltm
Russell v. McLellan, 53.	511.
v. M'Lellan, 234, 235, 237.	Sanbo
v. Temple, 8, 258.	San F
v. Waterworks Co., 393, 394, 401.	Mar
Rutherford v. Hill, 109.	Sanfo
Rutland Electric Light Co. v. Bates, 506.	Bro
Rutland & B. R. Co. v. Lincoln, 292.	Sange
v. Proctor, 169.	San
v. Thrall, 312, 320, 321, 324, 325, 327, 332, 364, 450.	We
Rutledge, Ex parte, 358.	Santa
Rutter v. Chapman, 52.	van
v. Kilpatrick, 817.	Sarge
R. W. Rogers Co. v. Wm. Rogers Manufacturing Co., 73.	v.
Ryan v. Dunlap, 497.	Sava
Ryder v. Railroad Co., 348.	Sava
Ryers v. South Australian Banking Co., 169.	404
	Sava
	191
	Savin
	Savin
	v.
	Saw
	v.
	Sayl
	v.
	Sayi
	v.
	Scan
	Schu
	Schu
	Schu
	Sch
	T
	4
Sabin v. Bank, 420.	
Safety Deposit Life Ins. Co. v. Smith, 113.	
Saffold v. Barnes, 287.	
Sage, In re, 337.	
v. Dillard, 214.	
Saint v. Manufacturing Co., 503.	
St. Clair v. Cox, 634-637.	

[The figures refer to pages.]

- Scheufler v. Grand Lodge**, 99.
Schickle v. Watts, 381.
Schley v. Dixon, 530, 608.
Schloss v. Trade Co., 97, 100, 102, 103, 106, 310.
Schoff v. Town of Bloomfield, 472.
Schollenberger, Ex parte, 638.
School Directors v. Carlisle Bank, 25.
School Dist. v. Insurance Co., 46.
School Dist. No. 61 v. Alderson, 101.
Schreyer v. Mills Co., 114, 115.
Schumm v. Seymour, 490.
Scott v. Armstrong, 554, 555, 557, 558.
 v. Bank, 417, 420, 425.
 v. Banking Co., 350.
 v. Depeyster, 518.
 v. Fire Co., 342, 343, 345, 348, 353, 563.
 v. Neely, 551.
Scovill v. Thayer, 360, 370, 371, 373, 587, 591, 601.
Scripture v. Soapstone Co., 424, 441.
Scruggs v. Mortgage Co., 625.
Seagraves v. City of Alton, 158.
Searsburgh Turnpike Co. v. Cutler, 9, 88.
Sedalia, W. & S. Ry. Co. v. Wilkerson, 279.
Seeley v. Bank, 346.
Sells v. Commission Co., 554.
Selma, M. & M. R. Co. v. Anderson, 286.
Selma & T. R. Co. v. Tipton, 88, 267, 321, 329, 335.
Semple v. Glenn, 84.
Sewall v. Power Co., 428.
Seymour v. Society, 181.
 v. Sturgess, 324.
Seymour Opera-House Co. v. Wooldridge, 68.
Shainwald v. Davids, 638.
Shakopee Manuf'g Co., In re, 62.
Shaw v. Mining Co., 75, 76, 77, 196, 438, 439, 526, 638.
 v. Spencer, 428, 429, 436.
Shea v. Mabry, 505.
Shellington v. Howland, 423, 598.
Shelton v. Banks, 50.
Shepaug Voting Trust Cases, 395, 480.
Sherman v. Smith, 216.
Sherman Center Town Co. v. Swigart, 483, 498.
Sherwood v. Alvis, 629.
 v. Mining Co., 429.
Shick v. Enterprise Co., 57.
Shickle v. Watts, 381, 603.
Shields v. Land Co., 102.
 v. Ohio, 215, 218.
Shober's Adm'rs v. Lancaster Co. Park Ass'n, 265.
Short v. Stevenson, 117.
Shortz v. Unangst, 52.
Shurtz v. Schoolcraft & Three Rivers R. Co., 293.
Sibley v. Bank, 424, 425.
Sicardi v. Oil Co., 609.
Silsby v. Barlow, 28.
Silver Hook Road v. Greene, 325.
Silver Lake Bank v. North, 190, 634.
Simm v. Telegraph Co., 437, 438.
Simmons v. Hill, 578.
Simons v. Mining Co., 117, 118.
Simpson v. Hotel Co., 138, 142, 393.
Sims v. Railroad Co., 277.
Singer Manuf'g Co. v. Peck, 58.
Sinking-Fund Cases, 214.
Skelly v. Bank, 202, 227.
Skinner v. Wilhelm, 39.
Skowhegan Bank v. Cutler, 424.
Skrainka v. Allen, 378.
Slater Woolen Co. v. Lamb, 172, 181, 182.
Slattery v. Transportation Co., 393, 401.
Slaughter v. Com., 617.
Slauson v. Schwabacher, 626, 627.
Slaymaker v. Bank, 258.
Slee v. Bloom, 236, 322, 330, 540, 542, 559, 561, 572, 599.
Sleeper v. Goodwin, 569, 573, 574, 584.
Slipher v. Earhart, 301.
Slocum v. Gas-Pipe Co., 100.
 v. Warren, 100.
Small v. Hydraulic Co., 321, 322.
Smith v. Association, 493, 510.
 v. Canal Co., 556.
 v. Hurd, 6, 391, 520, 535.
 v. Insurance Co., 640, 641.
 v. Law, 472.
 v. Manufacturing Co., 347, 639.
 v. Mining Co., 55.
 v. Mosby, 604.
 v. Nelson, 461.
 v. Plank-Road Co., 73.
 v. Poor, 608.
 v. Railroad Co., 551.
 v. Silver Val. Min. Co., 52.
 v. Warden, 110.
Smith's Appeal, 355.
Smith's Case, 237.
Smith's Estate, 357, 358.
Snell v. City of Chicago, 48.
Snider's Sons' Co. v. Troy, 97, 102, 104, 105, 108, 109.
Snyder v. Bank, 107.
 v. Studebaker, 44, 106.
Society for Propagating the Gospel v. Young, 73, 74.
Society for Propagation of Gospel in Foreign Parts v. Town of Pawlet, 48.
Society for the Propagation of the Gospel v. Town of New Haven, 30.
Society of Middlesex Husbandmen & Manufacturers v. Davis, 51, 53.
Society Perun v. Cleveland, 91, 97, 98, 107.
South Bay Meadow Dam Co. v. Gray, 100, 101, 217, 453.
Southern Hotel Co. v. Newman, 282.
Southern Life Ins. & Trust Co. v. Cole, 259.
 v. Lanier, 159, 316.
Southern Loan Co. v. Morris, 176.
Southern Pac. Co. v. Denton, 638.
Southern Pac. R. Co. v. Orton, 20, 44, 45.
South Nashville St. R. Co. v. Morrow, 222-224.

CASES CITED.

[The figures refer to

South School Dist. v. Blakeslee, 73.	State v
South Yorkshire Ry. & River Dun Co.	v.
v. Great Northern Ry. Co., 121.	v.
Spangler v. Railway Co., 324, 327.	v.
Spargo's Case, 379.	v.
Sparks v. Steel Co., 62.	v.
Spear v. Bach, 259.	v.
v. Crawford, 140, 262, 317, 319.	v.
v. Grant, 592.	v.
Spering's Appeal, 505, 515, 518, 607.	v.
Spiller v. Skating Rink Co., 114.	v.
Spooner v. Phillips, 356.	v.
Spague v. Manufacturing Co., 433, 442.	v.
Spring Valley Waterworks v. Schottler, 218.	v.
Stafford v. Mills Co., 640.	v.
Stafford Nat. Bank v. Palmer, 109.	
Standard Oil Co. v. Scofield, 150.	v.
Stanley v. Stanley, 210.	v.
Stanton v. Railway Co., 114.	
Starbuck v. Trust Co., 395.	v.
Starkweather v. Bible Society, 131, 168, 632.	v.
State v. Association, 59.	v.
v. Atchison & N. R. Co., 240.	v.
v. Bailey, 241.	v.
v. Baltimore, O. & O. R. Co., 198.	v.
v. Baltimore & O. R. Co., 347, 352, 353.	v.
v. Bank, 554.	
v. Bank of Maryland, 236.	v.
v. Beck, 57.	v.
v. Bergenthal, 337, 339.	v.
v. Bonnell, 466.	v.
v. Bull, 53.	
v. Cape Girardeau & S. L. R. Co., 45.	v.
v. Carey, 620, 633.	
v. Central Ohio Mut. Relief Ass'n, 57, 63.	
v. Central R. Co., 199.	
v. Chamber of Commerce, 402, 406, 404.	
v. Chicago, M. & St. P. Ry. Co., 199.	
v. Chute, 470, 481.	
v. Commercial Bank of Manchester, 240, 553.	
v. Commercial State Bank, 540.	
v. Commissioner of Railroad Taxation, 213.	
v. Corkins, 70.	
v. County Court, 47.	
v. Critchett, 56, 66, 92.	
v. Cumberland & P. R. Co., 224.	
v. Curtis, 40.	
v. Dawson, 44, 52.	
v. District Court of Ramsey Co., 636.	
v. Einstein, 337.	
v. Fidelity & Casualty Co., 622.	
v. Fidelity & Casualty Ins. Co., 623, 632, 633.	
v. Fourth New Hampshire Turnpike, 237, 238, 241, 242.	St
v. Great Works Milling & Manufacturing Co., 198.	St
v. Greer, 202, 204, 211, 479.	

[The figures refer to pages.]

- State Freight Tax Case, 225.
 State Ins. Co. v. Gennett, 424.
 v. Sax, 259, 424.
 State of Tennessee v. Whitworth, 223.
 State Railroad Tax Cases, 221.
 State Tax on Railway Gross Receipts, 226.
 State Treasurer v. Auditor General, 228.
 Steacy v. Railroad Co., 388, 411.
 Steam Nav. Co. v. Weed, 182, 631.
 Steamship Co. v. Murphy, 265.
 Steamship Dock Co. v. Heron's Adm'r, 413.
 Stebbins v. Jennings, 50.
 v. Merritt, 464, 465, 469, 471.
 Steger v. Davis, 181, 487.
 Stein v. Howard, 376, 377, 886.
 Stephens v. Follett, 578.
 v. Fox, 599.
 Steuart v. Bank, 9.
 Stevens v. Corbitt, 298.
 v. Davison, 455, 462.
 v. Iron Co., 496.
 v. Railroad Co., 392, 449.
 Stewart v. Jones, 143.
 v. Transportation Co., 400.
 Stewart Paper Manuf'g Co. v. Ran, 100.
 Stilling v. Town of Thorp, 31.
 Stockton Sav. Bank v. Staples, 129.
 Stoddard v. Foundry Co., 348.
 Stoffet v. Strome, 101, 106.
 Stone v. Kellogg, 337.
 v. Trust Co., 211.
 v. Wisconsin, 219.
 Stoneham Branch R. Co. v. Gould, 309, 310, 320.
 Story v. Furman, 588.
 v. Plank-Road Co., 213.
 Stourbridge Canal Co. v. Wheeley, 126.
 Stout v. Railroad Co., 76, 78, 80.
 v. Zulick, 88, 91, 108.
 Stoutimore v. Clark, 101.
 Stow v. Wyse, 465.
 Stowe v. Flagg, 35, 274.
 Stoystown & G. Turnpike R. Co. v. Craver, 490.
 Strasburg R. Co. v. Echternacht, 265.
 Struss v. Insurance Co., 172.
 Strubbling v. Bank, 84.
 Strong v. McCagg, 245.
 v. Railroad Co., 346, 347.
 Stuart v. Railroad Co., 280, 315.
 Sturges v. Carter, 223, 224.
 v. Vanderbilt, 89, 232, 249, 597.
 Stuts v. Handley, 378.
 Summers v. Sleeth, 317.
 Sumner v. Marcy, 151.
 Supreme Council v. Perry, 458.
 Susquehanna Canal Co. v. Bonham, 143.
 Susquehanna Mut. Fire Ins. Co. v. Elkins, 462.
 Sutton Manuf'g Co. v. Hutchinson, 542, 549.
 Sutton's Hospital Case, 13, 14, 35, 454.
 Swan Land & Cattle Co. v. Frank, 507.
 Swartwout v. Railroad Co., 97, 101, 105.
 Sweney v. Talcott, 58.
 Swift v. Smith, 67, 235.
 v. State, 337.
 v. Steamship Co., 139.
 Sykes v. People, 73.
 Symonds v. Board, 31.
 Symons' Case, 581.
 Syracuse City Bank v. Davis, 46.
- T
- Tabor v. Manufacturing Co., 625.
 Taft v. Railroad Co., 429, 435.
 Taft v. Railroad Co., 365, 366.
 v. Ward, 23.
 Taggart v. Railroad Co., 265, 296, 315, 331, 450.
 Talbot v. Scripps, 391.
 Talbott v. Casualty Co., 623.
 Talmage v. Peil, 128, 141, 151, 152.
 Tama Water-Power Co. v. Hopkins, 603.
 Tappan v. Bailey, 23.
 v. Bank, 224, 496.
 Tarbell v. Page, 101.
 Tar River Nav. Co. v. Neal, 321.
 Tatam v. Wright, 25, 616, 817.
 Tatam v. Rosenthal, 600.
 Tawas & B. C. R. Co. v. Iosco Circuit Judge, 546, 551.
 Taylor v. Bowker, 602.
 v. Earle, 445.
 v. Exporting Co., 154.
 v. Griswold, 455, 477, 479.
 v. Railroad Co., 372.
 Telegraph Co. v. Davenport, 435.
 v. Texas, 226, 618.
 Telfair v. Howe, 131.
 Temple v. Dodge, 459.
 Temple Street Cable Ry. Co. v. Hellman, 137.
 Templin v. Railway Co., 495.
 Ten Eyck v. Canal Co., 30.
 v. Railroad Co., 493, 511, 532.
 Tenney v. Protective Union, 28.
 Terrett v. Taylor, 27.
 Terry v. Little, 595.
 v. Tubman, 596, 599, 602.
 Thacher v. King, 610.
 Thayer v. Tool Co., 589.
 Thebus v. Smiley, 603.
 Thomas v. Board of Com'rs, 47.
 v. City of Richmond, 192.
 v. Dakin, 18, 14, 17, 19, 20, 37, 49.
 v. Railroad Co., 121, 135, 136, 144, 156, 167, 172, 189, 514.
 v. Railway Co., 47, 511, 512.
 Thompson v. Abbott, 556.
 v. Candoi, 88, 91, 94.
 v. Lambert, 142.
 v. Lumber Co., 554.
 v. Melser, 572, 590, 604.
 v. Waters, 129.
 Thomson v. Pacific R. R., 40.
 Thorne v. Insurance Co., 627.
 Thornton v. Balcom, 59.
 v. Railway Co., 49, 206, 233, 249.

[The figures refer to pages.]

Thorpe v. Railroad Co., 207-210.
 Thrasher v. Pike County R. Co., 273, 274.
 v. Railroad Co., 263.
 Throop v. Lithographic Co., 554, 555.
 Ticonic Water Power & Manuf'g Co. v. Lang, 281, 292, 298.
 Tift v. Bank, 113, 115.
 Tinsman v. Railroad Co., 80.
 Tisdale v. Harris, 259.
 Titcomb v. Insurance Co., 252, 260.
 Titus v. President, etc., 438.
 v. Railroad Co., 495.
 v. Turnpike Road, 526.
 Todd v. Birdsall, 32.
 Toledo Tie & Lumber Co. v. Thomas, 627.
 Toledo & Ann Arbor R. Co. v. Johnson, 61, 243.
 Tolford v. Church, 38.
 Tome v. Railroad Co., 196, 438, 526.
 Tomkinson v. Railway Co., 135, 137.
 Tomlinson v. Bricklayers' Union No. 1, 7, 391.
 v. Jessup, 228.
 Tonica & P. R. Co. v. McNeely, 265, 268.
 Topping v. Bickford, 157, 159.
 Torrey v. Association, 496.
 Totten v. Tison, 362, 363, 367.
 Towers Excelsior & Ginnery Co. v. Inman, 182.
 Town v. Bank of River Raisin, 554.
 Town of Lake View v. Rose Hill Cemetery Co., 208, 209.
 Town of McGregor v. Baylies, 45.
 Town of New Athens v. Thomas, 158.
 Town of North Hempstead v. Town of Hempstead, 32, 50.
 Town of St. Albans v. National Car Co., 222, 224.
 Townsend v. Turnpike Road, 195.
 Tracy v. Talmage, 192.
 Treadwell v. Manufacturing Co., 153, 445.
 Trevor v. Whitworth, 153, 154.
 Tripp v. Bank, 486.
 Trowbridge v. Scudder, 109.
 Troy & B. R. Co. v. Tibbits, 279, 300.
 Troy & G. R. Co. v. Newton, 297, 309, 312.
 Trustees v. Flint, 459, 559.
 Trustees of Cincinnati Tp. v. Ogden, 158.
 Trustees of Dartmouth College v. Woodward, 29, 30, 35, 202, 203.
 Trustees of Phillips Academy v. King, 29, 133.
 Trustees of School Dist. No. 3 v. Gibbs, 482.
 Trustees of Schools v. Tatman, 30.
 Trustees of Soldiers' Orphans' Home v. Shaffer, 461.
 Trustees of the First Society of the Methodist Episcopal Church of Newark v. Clark, 102.
 Trustees of University v. Winston, 30.

Trustees of Vernon Soc. v. Hills, 237, 243.
 Tuckahoe Canal Co. v. Tuckahoe & J. River R. Co., 205, 212.
 Tucker v. Ferguson, 228.
 Tunesma v. Schuttler, 597.
 Tunis v. Railroad Co., 472, 476, 479.
 Turnbull v. Lumber Co., 552, 553.
 v. Payson, 577.
 Turner v. Insurance Co., 196, 284.
 Turnpike Co. v. Wallace, 29.
 Twin-Lick Oil Co. v. Marbury, 511, 512, 513.
 Tyrell v. Washburn, 23.

U

Umsted v. Buskirk, 592.
 Underhill v. Improvement Co., 461, 462.
 Union Bank v. Jacobs, 138, 147.
 v. Laird, 414, 420, 421.
 Union Cent. Life Ins. Co. v. Thomas, 626.
 Union Gold Min. Co. v. Rocky Mountain Nat. Bank, 145.
 Union Hardware Co. v. Plume & Atwood Manuf'g Co., 181.
 Union Hotel Co. v. Hersee, 297, 309, 450.
 Union Iron Co. v. Pierce, 611.
 Union Loan & Trust Co. v. Southern California Motor-Road Co., 376.
 Union Mut. Life Ins. Co. v. Frear Stone Manuf'g Co., 305, 370, 373.
 v. McMillen, 627, 628.
 Union Nat. Bank v. Byram, 260.
 v. Hunt, 287.
 Union Pac. R. Co. v. Lincoln Co., 40.
 v. U. S., 217.
 Union Passenger Ry. Co. v. Philadelphia, 229.
 Union Sav. Ass'n v. Seligman, 585.
 Union Switch & Signal Co. v. Hall Signal Co., 639.
 United Society of Shakers v. Underwood, 516, 607.
 U. S. v. City Bank, 497.
 v. E. C. Knight Co., 240.
 v. Knox, 567.
 v. Memphis & L. R. R. Co., 200.
 v. Southern Pac. R. Co., 638.
 U. S. v. Vaughan, 426.
 United States Bank v. Stearns, 84.
 United States Mercantile Reporting & Collecting Agency, In re, 73.
 United States Rolling-Stock Co. v. Atlantic & G. W. R. Co., 510, 511, 513.
 United States Trust Co. v. United States Fire Ins. Co., 584, 585, 604.
 United States Vinegar Co. v. Schlegel, 83.
 Unity Ins. Co. v. Cram, 56.
 Upton v. Englehart, 289, 290.
 v. Hansbrough, 88, 100.
 v. Tribilcock, 287, 290, 305, 319, 330, 373, 561.

[The figures refer to pages.]

Utley v. Mining Co., 625.
v. Tool Co., 56, 60, 94.

V

Vall v. Hamilton, 475.
v. Jameson, 554.
Valley Ry. Co. v. Lake Erie Iron Co., 151.
Van Aernam v. Bleistein, 24.
Van Allen v. Assessors, 230.
Vance v. Coke Co., 540, 550.
Van Cott v. Van Brunt, 376, 387.
Vanderpoel v. Gorman, 486.
Vanderwerken v. Glenn, 601.
Van Dyck v. McQuade, 353, 515, 607.
Van Houten v. McKelway, 28.
Van Kirk v. Clark, 32.
Vanneman v. Young, 58.
Van Norman v. Jackson Circuit Judge, 259, 260.
Vansands v. Bank, 458.
Varnum v. Hart, 554.
Vater v. Lewis, 101.
Vawter v. Griffin, 259.
Veeder v. Mudgett, 360, 568, 587.
Vent v. Spice Co., 153.
Vermont Cent. R. Co. v. Claves, 315.
Verplanck v. Insurance Co., 245.
Vestry of St. Luke's Church v. Mathews, 456, 458.
Vidal v. Mayor, etc., 133.
Vincennes University v. State of Indiana, 40.
Visalia Gas & Electric Light Co. v. Sims, 189.
Von Phue v. Hammer, 47.
Voorhis v. Terhune, 260.
Vowell v. Thompson, 475.
Vreeland v. Stone Co., 277, 278, 284.

W

Wadesboro Cotton Mills Co. v. Burns, 100.
Wahlig v. Manufacturing Co., 496, 501.
Wakefield v. Fargo, 573.
Wakeman v. Dalley, 531.
Walburn v. Chenault, 380.
Walker v. Detroit Transit Ry. Co., 441.
v. Devereaux, 277.
v. Railroad Co., 284, 285, 287, 288, 429, 431.
Wall v. Society, 625.
Wallace v. Loomis, 44, 45.
v. Townsend, 268, 269.
Walstab v. Spottiswoode, 112.
Walter A. Wood Harvester Co. v. Robins, 262, 267, 317.
Walton v. Riley, 58.
Walworth v. Brackett, 61.
Walworth County Bank v. Farmers' Loan & Trust Co., 495.
Ward v. Brigham, 109.
v. Farwell, 208, 211, 240.
v. Johnson, 147.
v. Railroad Co., 89.

Wardell v. Railroad Co., 506, 509, 511, 514.
Wardens of Christ Church v. Pope, 482.
Wardle v. Townsend, 39.
Ware v. Shoe Co., 618.
Warfield v. Canning Co., 554.
Waring v. Catawba Co., 8.
Warner v. Beers, 2, 15, 18, 19, 21, 23.
v. Mower, 465, 472.
Warren v. Insurance Co., 6.
v. King, 365.
Washburn v. Green, 378.
Washburn Mill. Co. v. Bartlett, 626, 629.
Washington Ins. Co. v. Price, 9.
Washington Sav. Bank v. Butchers' & Drovers' Bank, 594, 601.
Washington & B. Turnpike Co. v. Baltimore & O. R. Co., 205.
Waterbury v. Express Co., 245, 400.
Watson v. Jones, 28.
Watt's Appeal, 400, 507, 515, 607.
Wayne Pike Co. v. Hammons, 393, 505, 520.
Weatherford, M. W. & N. W. Ry. Co. v. Granger, 113-116.
Webb v. Railroad Co., 259, 278, 296-298, 315, 317.
v. Ridgely, 476.
Webber v. College, 496.
Webster v. Upton, 330, 411.
Wechselberg v. Bank, 110.
Weckler v. Bank, 135, 137, 502, 526, 528.
Weeks v. Love, 596, 597.
Weinman v. Railway Co., 47, 100, 107.
Weiss v. Iron Co., 263.
Welch v. Bank, 513.
Welland Canal Co. v. Hathaway, 103.
Welles v. Larrabee, 583-585.
Wellington & P. R. Co. v. Cashie & C. R. & L. Co., 89.
Wells v. Gates, 22, 23.
v. Rodgers, 328.
Wells, Fargo & Co. v. Northern Pac. R. Co., 68, 70.
Wemple v. Railroad Co., 278, 317.
Wenlock v. River Dee Co., 145, 179.
Wert v. Turnpike Co., 287.
West v. Crawford, 272, 310.
v. Ditching Co., 57.
West Chester & P. R. Co. v. Jackson, 351, 363.
Western Bank of Scotland v. Addie, 285.
Western News Co. v. Wilmarth, 196.
Western Screw & Manuf'g Co. v. Conley, 113.
Western Union Tel. Co. v. Davenport, 428, 429.
Westervelt v. Demarest, 531.
Westman v. Krumweide, 307.
Weston v. Hunt, 27.
v. Mining Co., 424.
Weston's Case, 407, 581.
West River Bridge Co. v. Dix, 212.
West Wisconsin Ry. Co. v. Board of Sup'rs., 227, 228.

[The figures refer to pages.]

Wetherbee v. Baker, 381, 592, 598.
Weyer v. Bank, 430.
Wheeler v. Millar, 604.
 v. Sleigh Co., 343, 349, 355.
Wheeler, Osgood & Co. v. Everett Land Co., 149.
Wheeler & W. Manuf'g Co. v. Boyce, 194, 197, 527.
Wheelock v. Kost, 100, 584.
 v. Moulton, 7, 8.
Whipple v. Parker, 110.
Whitaker v. Canal Co., 127.
 v. Masterton, 610.
Whitbeck v. Bank, 227.
White v. Bank, 177, 189, 192.
 v. Howard, 131, 631, 632.
 v. Railroad Co., 146, 453.
Whitehill v. Jacobs, 380, 383.
White Mountains R. Co. v. Eastman, 305, 330, 373.
White River Turnpike Co. v. Vermont Cent. R. Co., 205, 212.
White Water Valley Canal Co. v. Boden, 84.
 v. Vallette, 146.
Whitman Agricultural Co. v. Strand, 628.
Whitney v. Butler, 580, 581.
 v. City of Madison, 224.
 v. Robinson, 88, 101.
 v. Wyman, 104, 114.
Whitney Arms Co. v. Barlow, 137, 180, 181, 183, 610.
Whittemore v. Gibbs, 259.
Whittenton Mills v. Upton, 150.
Wickersham v. Zinc Co., 504.
Wiggin v. Elder, 465.
Wight v. Railroad Co., 287, 288, 301, 307, 315, 484.
Wild v. Bank of Passamaquoddy, 497.
Wilde v. Jenkins, 235.
Wiles v. Suydam, 575, 611.
Wilkins v. Thorne, 639.
Wilkinson v. Bauerle, 486, 512, 515, 553, 554, 607-609.
Willamette Freighting Co. v. Stannus, 310.
Willcocks, Ex parte, 470, 475.
Williams v. Bank, 23, 48, 84, 419, 424.
 v. Cheney, 629.
 v. Evans, 385, 387.
 v. Hewitt, 104, 110.
 v. McDonald, 516, 607.
 v. McKay, 518.
 v. Manufacturing Co., 154.
 v. Taylor, 324, 601.
 v. Telegraph Co., 256, 847, 850, 351.
 v. Traphagen, 608.
Williams' Case, 583.
Williamson v. Association, 88, 91, 97.
 v. Smoot, 7, 614.
Willis v. Chapman, 23, 52.
 v. Mabon, 567, 569, 570.
Williston v. Railroad Co., 353, 365, 366.
Wilmington R. R. v. Reid, 227.
Wilmington & W. R. Co. v. Alsbrook, 228.

Wilson v. Fire-Alarm Co., 635.
 v. Proprietors Central Bridge, 475.
Winch v. Railway Co., 144.
Wincham Ship-Building, Boiler & Salt Co., In re, 609.
Wincock v. Turpin, 597, 605.
Windsor Electric Light Co. v. Tandy, 318, 319.
Wing v. Slater, 570.
Winget v. Association, 92, 101, 107.
Winston v. Brooks, 305.
Winter v. Baldwin, 339.
Winter v. Montgomery Gaslight Co., 422, 430.
Winters v. Armstrong, 309.
Wisconsin Tel. Co. v. City of Oshkosh, 70.
Witte v. Fishing Co., 159.
Witters v. Sowles, 586.
Wolfe v. Underwood, 347.
Wolters v. Henningsan, 605.
Wood v. Dummer, 345, 373, 539, 540, 542, 543, 563, 564.
 v. Hammond, 168.
Woodbury v. Railroad Co., 147.
Woodbury Heights Land Co. v. Loudenslager, 117, 119.
Woodruff v. McDonald, 281.
 v. Railroad Co., 480.
Woodruff's Estate, In re, 857.
Worcester Medical Inst. v. Harding, 101.
Worcester Turnpike Corp. v. Willard, 267, 321.
Wright v. Hughes, 139, 142, 145, 165, 181, 184.
 v. Lee, 88, 105, 447, 468, 486, 491, 614, 626, 629.
 v. McCormack, 598.
 v. Pipe Line Co., 181, 182.
 v. Railroad Co., 223.
 v. Water Co., 472, 478, 534.
Wyles v. Suydam, 602.

Y

Yakima Nat. Bank v. Knipe, 84.
Yale Gas-Stove Co. v. Wilcox, 117.
Yanish v. Fuel Co., 161.
Yarborough v. Bank, 193, 194.
Yardley v. Wilgus, 586.
Yenton v. Bank of Old Dominion, 52, 53, 213, 214.
Yellowjacket Silver Min. Co. v. Stevenson, 490.
York Park Bldg. Ass'n v. Barnes, 70, 277, 305.
York & M. L. R. Co. v. Winans, 189.
Young v. Iron Co., 260, 380, 388.
 v. McKay, 581.
Younglove v. Lime Co., 572, 598, 599, 602.

Z

Zabriskie v. Railroad Co., 204, 216, 398, 397, 448, 449, 453.
Zimmer v. State, 202, 208.
Zinn v. Mendel, 530, 531, 608.

INDEX.

[THE FIGURES REFER TO PAGES.]

A

ABANDONMENT,

- of charter, 235.
- of business and franchises, 236.
- of articles of association, 282.

ABATEMENT AND REVIVAL,

- see "Actions."

ABUSE OF POWER,

- see "Forfeiture of Charter"; "Officers and Agents"; "Powers and Liabilities of Corporation."

ACCEPTANCE,

- of charter, 50-54.
- of amendment of charter, 53, 54, 218.
- presumption from conduct, 51, 53.
- power of majority to accept amendment of charter, 444, 447.
- of subscription to stock, 261, 264.
- by state of surrender of charter, 285.

ACCOMMODATION PAPER,

- power of corporation to execute, 134, 148.
- negotiable paper, bona fide purchasers, 175.

ACCOUNTING,

- by officers, see "Officers and Agents."

ACTIONS,

- power of corporation to sue, 122.
- between the corporation and its members, 8.
- by stockholder against corporation for dividend, 341, 351.
- against corporation for refusal to recognize transfer of shares, 440.
- by corporation on subscriptions, 318-321.
- by and against corporation after dissolution, 249.
- by corporation against officers and agents, 514, 519.
- by stockholders against officers and agents, 534.
- by stockholders for injuries to corporation, and interference in management, 7, 11, 389-401.
- at law, 7, 389, 391.

[The figures refer to pages.]

ACTIONS—Continued,

- in equity, 11, 389, 392.
- acts within power of majority, and discretionary powers, 395.
- the rule as stated by the United States supreme court, 398.
- laches and estoppel, 399.
- motive of stockholder suing, 400.
- parties to suits, 400.
- abatement and revival, dissolution of corporation, 249.
- action to enforce liability of stockholder to creditors, 587.
- by and against foreign corporations, 633 et seq.
- by creditors of corporation, see "Creditors of Corporations."

AGENCY,

- subscriptions by agent, 291.
- effect of want of authority, 291.
- agents of corporation, see "Officers and Agents."

AGGREGATE CORPORATIONS,

- in general, 1, 28.
- see "Corporations."

AGREEMENTS,

- between corporators, 64.
- between corporators and the corporation, 64.
- between corporation and the state, acceptance of charter, 50-54.
- see "Contracts"; "Stockholders and Members."

ALIENS,

- as corporators, 66.
- as subscribers to stock, 275.

ALLOTMENT,

- of shares, 318.

ALTERATION,

- of subscription, 282.
- of charter, see "Amendment"; "Majority"; "State Control."

AMENDMENT,

- of charter, power of state, see "State Control."
- acceptance, 53, 54, 213.
- general and special laws, 44, 45.
- as a release of subscribers, 331.
- to authorize preferred stock, 364.
- power of majority, 444, 447.
- of by-laws, 461.

[The figures refer to pages.]

AMOTION,

- of officers, 582.
- by-laws, 455.
- expulsion of members, 401-405.

APPOINTMENT,

- of agents, see "Officers and Agents."

ARTICLES OF ASSOCIATION,

- necessity for, and sufficiency, 56 et seq.
- filing or recording, 57.
- publishing, 57.
- see "Charters"; "Creation of Corporations"; "De Facto Corporations"; "Estoppel."

ASSAULT AND BATTERY,

- see "Torts."

ASSESSMENTS AND CALLS,

- in general, 322-327.
- necessity, 323.
- validity, 325.
- notice and demand, 327.
- interest, 327.
- action by corporation, 318-321.
- liability after transfer of shares, 410.

ASSETS,

- as a trust fund, see "Creditors of Corporations."

ASSIGNMENT,

- of unpaid subscription to stock, 328.
- by corporation for benefit of creditors, 553.
- of shares, see "Transfer of Shares."

ASSUMPSIT,

- see "Actions."

ATTACHMENT,

- of shares of stock, 257, 259.
- of corporate property, 538.
- of property of foreign corporation, 636.

ATTRIBUTES,

- of corporation, 12 et seq.

[The figures refer to pages.]

B

BANKING CORPORATIONS,

- powers, lending money, 128.
- buying notes, etc., 128.
- purchase of real or personal property, 140, 141.
- see heading relating to particular point.

BEQUEST,

- income and profits of shares, 354.

BILLS AND NOTES,

- see "Contracts."

BOARD OF DIRECTORS,

- see "Officers and Agents."

BONDS,

- see "Contracts."

BONUS STOCK,

- see "Watered and Bonus Stock."

BOOKS,

- inspection by stockholders or members, 336-339.
- as evidence, see "Evidence."

BORROWING,

- see "Contracts."

BY-LAWS,

- in full, 454-462.
- by whom enacted, 454.
- must be proved, not judicially noticed, 455.
- validity, 455 et seq.
- providing for election, appointment, and removal of officers, 455.
- limiting powers and prescribing duties of officers and agents, 455, 497.
- provision for corporate meetings, 455.
- regulating right to vote, 455.
- regulating transfer of shares, 407, 455, 457.
- providing for expulsion of members, 456.
- must be consistent with law, 456.
- restraint of trade, 456.
- giving lien on shares, 413, 457.
- providing for forfeiture of shares, 456, 458.
- must be reasonable, 455, 456.
- must be general, 456.
- must be consistent with charter, 458.
- cannot deprive stockholder of contract rights, 459.

[The figures refer to pages.]

BY-LAWS—Continued,

- partial invalidity, 459.
- effect as to stockholders, 460.
- effect as to third persons, 460.
- repeal and amendment, 461.
- waiver of by-laws, 462.
- violation by officers, liability to corporation, 518.

O

CALLS AND ASSESSMENTS,

- in general, 322-327.
- necessity, 323.
- validity, 325.
- notice and demand, 327.
- interest, 327.
- action by corporation, 318-321.
- liability after transfer of shares, 410.

CAPACITY,

- of corporators, 64.

CAPITAL STOCK,

- defined, 256.
- increase of, 358.
 - subscriptions and payment thereof, 359.
 - unauthorized increase, 360.
 - shareholder's right to preference, 360.
- preferred stock, 361-368.
 - defined, 361, 362.
 - power to create, 361, 362.
 - amendment of charter authorizing, 364.
 - laches and estoppel of stockholders, 364.
 - rights and liabilities of holders of, 365.
 - dividends, 365.
 - liability to creditors, 367.
 - status as creditors and not stockholders, 365, 367.
- watered and bonus stock, 368-389.
 - defined, 368.
 - effect as to corporation, 368, 369.
 - effect as to stockholders, 368, 371.
 - effect as to creditors, 368, 372.
 - payment of original subscriptions, 368, 372.
 - increase of capital stock, 368, 374.

[The figures refer to pages.]

CAPITAL STOCK—Continued,

issue of stock at market value by active corporation to pay debts, etc., 368, 375.

gratuitous issue of stock, 369, 378.

payment for stock in property or services, 369, 379.

value of property or services, 369, 379.

creditors who cannot complain, 369, 388.

effect of constitutional and statutory provisions, 369, 384.

liability of transferees, 388.

power of corporation to acquire and hold stock, 134, 151-153.

certificates of stock, see "Certificates."

subscriptions, see "Subscriptions to Stock."

transfer, see "Transfer of Shares."

as a trust fund, see "Creditors of Corporations."

CASHIER,

see "Officers and Agents."

CERTIFICATES,

of incorporation, necessity for and sufficiency, 56 et seq.

filing or recording, 57.

publishing, 57.

see "De Facto Corporations"; "Estoppel."

of stock, nature of, 260, 316.

not necessary to membership in corporation, 260, 316.

new certificate on transfer of shares, 427.

compelling issuance, 441.

forged and unauthorized certificates, 427, 434, 437.

liability of indorser, 434.

liability of corporation, 437.

CHARITABLE CORPORATIONS,

nature, 26, 28.

CHARTER,

authority from the state essential to corporate existence, 33.

power to grant charter, 33.

power of state legislatures, 34.

grant of exclusive privileges, 36.

enactment of acts, two-thirds vote, 37.

restriction as to subject and title of acts, 37.

restrictions in federal constitution, 37, 38.

power of congress, 34, 39.

corporations in District of Columbia, 40.

power of territorial legislatures, 34, 40.

presumption of charter, prescription, 34, 35.

[The figures refer to pages.]

CHARTER—Continued,

- delegation of power to create corporations, 34, 40.
- performance of ministerial acts, 34, 41.
- general and special laws, 42-48.
 - limitation on power of territorial legislature, 40.
 - distinction between general and special law, 42.
 - conferring additional privileges or powers, 42, 44.
 - amendment of charter, 44, 45.
 - "special" law defined, 46.
- ratification of claim to corporate existence, 48.
- intention to create a body corporate, 49.
- acceptance of charter, 50-54.
- withdrawal or repeal of offered charter or enabling act, 50, 52.
- presumption of acceptance, 51, 53.
- who may accept, 52.
- acceptance of amendment, 53.
 - who may accept, 54.
 - see "Amendment."
- place of organization, outside the state, 54.
- compliance with conditions precedent, 55-63.
 - substantial compliance sufficient, 55, 59.
 - directory provisions, 55, 60.
 - conditions subsequent, distinguished, 56, 61.
 - who may object, de facto corporations, 56, 62.
 - estoppel, 56, 62.
- particular conditions, 56-62.
- surrender, 235.
- extension of, 81.
 - distinguished from creation of new corporation, 81.
 - effect, 81.
- expiration, 89, 232.
- construction of, in general, 124.
 - in favor of the public in cases of doubt, 125.
 - general terms following special terms, 125, 127.
 - express mention and implied exclusion, 125, 128, 129.
 - intention to create a body corporate, 49.
 - purpose of incorporation, 67, 69.
 - see "Powers and Liabilities."
- forfeiture, see "Dissolution"; "Forfeiture of Charter."
- as a contract not to be impaired, see "State Control."
- amendment, see "Amendment."

CITIZEN,

- corporation as a, 24.
- Clk.Pr.Corp.—44

[The figures refer to pages.]

CITIZENSHIP,

of corporation, 74-80.

for purpose of jurisdiction of federal courts, 75-80.

where there are charters from several states, 75, 77.

charter distinguished from license, 75, 80.

see "Foreign Corporations."

CIVIL CORPORATION,

defined, 26, 28.

COMPANIES,

see "Corporations"; "Joint-Stock Company."

COMPENSATION,

of officers, 581.

CONDITIONS PRECEDENT,

to formation of corporation, 55-63.

substantial compliance sufficient, 55, 59.

directory provisions, 55, 60.

conditions subsequent, distinguished, 56, 61.

who may object, de facto corporations, 56, 62.

estoppel, 56, 62.

particular conditions, 56-62.

in contract of subscription, 294-302.

after incorporation, 296.

prior to incorporation, 299.

must be expressed in the writing, 301.

waiver, 301.

distinguished from special terms, 295, 302.

CONDITIONS SUBSEQUENT,

distinguished from conditions precedent to incorporation, 61.

in subscriptions to stock, 302.

distinguished from conditions precedent, 295, 302.

validity, 304.

who may receive, 306.

CONFLICT OF LAWS,

power to take and hold property, 181.

transfer of shares, 417.

CONGRESS,

power to create corporations, 34, 39.

in District of Columbia, 34, 40.

CONSIDERATION,

for subscription to stock, 267, 271.

[The figures refer to pages.]

CONSOLIDATION,

power of corporations to consolidate, 136.
effect as to creditors, 556.

CONSPIRACY,

liability of corporations, 193, 196.
see "Torts."

CONSTITUTIONAL LIMITATIONS,

on power of state legislatures to create corporations, 34, 37.
requirement of two-thirds vote, 37.
restrictions as to subject and title of acts, 87.
grant of exclusive privileges, 36.
general and special laws, 42-48.
distinction, 42.
conferring additional privileges or powers, 42, 44.
"special" law defined, 46.
restrictions of federal constitution, 87, 88.
power of congress to create, 34, 39.
in District of Columbia, 34, 40.
federal corporation not controllable by states, 40.
territorial corporations, 34, 40.
delegation of power to create corporations, 34, 40.
performance of ministerial acts, 34, 41.
the charter as a contract not to be impaired, see "State's Control."
impairing rights of creditors, 574, 575.

CONSTRUCTION,

of charters, see "Charters."

CONTINUOUS SUCCESSION,

the attribute of, 12, 15.

CONTRACTS,

power to contract, in general, 120 et seq., 133.
purchase of real and personal property, 128, 135-142.
sale, conveyance, lease, mortgage, or pledge, 134, 136, 138, 142.
railroad and other quasi public corporations, 134, 136, 138, 143.
sale or mortgage of franchise, 134, 143.
borrowing money, 134, 145.
executing bonds, 134, 146.
negotiable instruments, 134, 147.
suretyship and guaranty, 134, 136, 148.
accommodation paper, 134, 148.
contracts of partnership, 134, 150.
joint contracts, 134, 151.

[The figures refer to pages.]

CONTRACTS—Continued,

- subscription for or purchase of stock in another corporation, 134, 151.
- taking and holding stock to secure, or in payment of debt, 134, 152.
- purchase of its own stock, 135, 153-155.
- taking and holding stock to secure, or in payment of debt, 135, 154.
- presumption of power to contract, 135, 155.
- lending money, 123.
- subscription to expenses of festival, etc., 137.
- offer of reward for apprehension of criminals, 138.
- form and mode of corporate contracts, 156-162.
- seal, 19, 156, 157, 160.
- effect of seal, 162.
- appointment of agent, 157.
- implied contracts, 158.
- quasi contract, 158.
- requirement of writing, 159.
- effect of ultra vires contract, see "Ultra Vires."
- illegal contracts, see "Ultra Vires."
- of members, not binding on corporation, 7.
- between corporators, 64.
- between corporators and the corporation, 64.
- between the corporation and the state, acceptance of charter, 50-54.
- the charter as a contract not to be impaired, see "State Control."
- by promoters, 111, 112, 117.
- subscriptions, see "Subscriptions to Stock."
- for sale of shares, statute of frauds, 258, 259.
- between stockholder or member and corporation, 8, 504.
- between officers and corporation, 508 et seq.
- liability of officers and agents to third persons, 521.
- of foreign corporations, 632.

CONTRIBUTION,

- between stockholders, 604.

CONVEYANCES,

- of corporate property by members, 6, 7.
- between members and the corporation, 8.
- power to take, 123, 135-142.
- power to make, 134, 136, 138, 142.
- railroad and other quasi public corporations, 134, 136, 138, 143.
- conveyance of franchise, 134, 143.

CORPORATE ENTITY,

- explained, 5 et seq.

[The figures refer to pages.]

CORPORATE NAME,

in general, 17, 122.

CORPORATION,

defined, 1.

as a legal entity, 5, 16.

as a collection of individuals, 9.

attributes and incidents, 12.

distinguished from partnership, 12 et seq.

from unincorporated joint stock company, 21.

as a person, citizen, inhabitant, etc., 24.

kinds of corporations, 26.

sole and aggregate, 26, 27.

religious or ecclesiastical, 26, 28.

eleemosynary, 26, 28.

civil, 26, 28.

public and private, 26, 29.

stock and nonstock, 26, 31.

quasi corporations, 26, 31.

by prescription, 34, 36.

de facto, see "De Facto Corporations."

foreign corporations de facto, 632.

distinction between corporation and its members, 1-11.

CORPORATORS,

agreement between, 64.

agreement between corporators and corporation, 64.

who may become, 64.

number of, 56, 64.

see "Stockholders or Members."

COVERTURE,

see "Married Women."

CREATION OF CORPORATIONS,

in general, 33 et seq.

power to create, 33.

state legislatures, 34, 36.

congress of the United States, 34, 39.

in District of Columbia, 34, 40.

territorial legislatures, 34, 40.

corporations by prescription, 34, 35.

delegation of power, 34, 40.

general and special laws, 42.

constitutional restriction, 43.

ratification of claim to corporate existence, 43.

[The figures refer to pages.]

CREATION OF CORPORATIONS—Continued,

- intention to create, 49.
- agreement between corporation and the state, acceptance of charter, 50.
- place of organization, 54.
- compliance with conditions precedent, 55.
- articles of association or certificate, necessity and sufficiency, 56 et seq.
 - filing or recording, 57.
 - publishing, 57.
 - see "De Facto Corporations"; "Estoppel.
- agreement between corporation and corporators, 64.
- who may become corporators, 64.
- number of corporators, 64, 66.
- purpose of incorporation, 67.
- corporations in restraint of trade, 67, 71.
- corporate name, 71.
- residence and citizenship of corporations, 74.
- corresponding charters in several states, 74, 77.
- recognition of foreign corporation distinguished, 74, 80.
- extension of charter or creation of new corporation, 81.
- proof of corporate existence, 82.
 - for particular questions, see specific heads.

CREDITORS OF CORPORATIONS,

- relation between creditors and the corporation, 537-557.
 - remedies in general, 537.
 - property subject to execution, 538.
 - assets of a corporation as a trust fund for creditors, 539-546.
 - interference in management of corporation, 546.
 - fraudulent conveyances and transfers, 549.
 - subsequent creditors, 550.
 - necessity for judgment before attacking, 551.
 - suits for injunction and receiver, 552.
 - assignment for benefit of creditors, 553.
 - right to prefer creditors, 553.
 - dissolution of corporation, effect, 555.
 - effect of consolidation of corporations, 556.
 - extension of charter, new corporation, 556.
 - set-off by debtor of corporation, 557.
- relation between creditors and stockholders, 558-605.
 - liability of stockholders to creditors at common law, 18, 558-564.
 - liability on subscriptions, 559-562.
 - conditional subscriptions, 560.
 - subscriptions on special terms, 560.
 - release of subscriber by corporation, 561.

[The figures refer

CREDITORS OF CORPORATIONS—C

liability of holders of watered o
original subscriptions, 368, 1
increase of capital stock, 36
issue of stock at market va
etc., 368, 375.
gratuitous issue of stock, 3
payment for stock in prop
value of property or servic
creditors who cannot comp
effect of constitutional and
liability of transferees, 382
rights as to profits and divid
diversion of capital, unauthor
preferred stockholders, 387, 56
statutory liability of stockholders
may be excluded by express a
unpaid installment of subscri
unlimited statutory liability, 5
limited liability, 567.
liability until capital is paid in
constitutional provisions, 569.
effect of dissolution of corpor
nature of liability, whether r
nature of contractual liability
what constitutes dissolution f
"debts," "demands," etc., wit
debts due clerks, laborers, et
excepted classes of corporati
release or discharge of corpe
constitutional law, laws affe
repeal or change of law,
extraterritorial effect of statute
who liable as stockholders u
general rule, 577.
shares registered in nam
effect of transfer of sha
registration of trans
transfer to person in
to infant, 581.
to corporation, 581.
to insolvent, 582.
sham or colorable tr

[The figures refer to pages.]

CREDITORS OF CORPORATIONS—Continued,

- transfers after suspension of business, 583.
- pledgees, 583.
- trustees, executors, agents, etc., 585.
- election between apparent and real owner, 586.
- assignees in bankruptcy or insolvency, 586.
- married women, 586.
- death of stockholder, survival of liability, 587.
- forfeiture of stock, 587.
- holders of unauthorized stock, 587.
- status of preferred stockholders, whether creditors, 586, 587.
- who may enforce statutory liability, 588.
- stockholders or officers who are creditors, 588.
- remedies of creditors against stockholders, 589.
- common-law liability on subscriptions, etc., 590.
- action by assignee for creditors or in bankruptcy, 590.
- action at law by creditors, 591.
- general creditors' bill in equity, 591.
- suit for appointment of receiver, 591.
- parties to suit, 592.
- necessity for calls, 593.
- statutory remedies, 594.
- statutory liability, 594.
- where the statute gives a remedy, 594.
- where no remedy is prescribed, 595.
- necessity for judgment against corporation, 597.
- effect of judgment against corporation, 599.
- statute of limitations, 600.
- liability on subscription, 600.
- statutory liability, 601.
- set-off by stockholders, 602.
- contribution among stockholders, 604.
- relation between creditors and officers, 605-611.
- liability of officers to creditors at common law, 606.
- preferences to officers who are creditors, 608.
- statutory liability, 609.

CRIMES,

- responsibility of corporation, 197.

CUMULATIVE VOTING,

- at stockholders' meetings, 478.

CURATIVE ACTS,

- ratifying claim to corporate existence, 48.

[The figures refer to pages.]

D

DEBTS,

see "Powers and Liabilities."

DECEIT,

see "Torts."

DEEDS,

see "Contracts"; "Conveyances."

DE FACTO CORPORATIONS,

defined, 86.

status and powers, 86, 87.

foreign de facto corporations, 88, 632.

de facto existence after expiration of charter, 89.

what necessary to constitute, 90-98.

valid law authorizing incorporation, 92.

bona fide attempt to organize, 62, 93.

sufficiency of compliance with law, 94.

user of corporate powers, 95.

fraudulent attempt to organize, 96.

doctrine is distinct from doctrine of estoppel, 96.

see "Estoppel."

DE FACTO DIRECTORS,

see "Officers and Agents."

DEFINITIONS,

corporation, 1.

unincorporated joint-stock company, 21.

sole corporation, 26, 27.

aggregate corporation, 1, 26, 27.

religious corporation, 26, 28.

ecclesiastical corporation, 26, 28.

eleemosynary corporation, 26, 28.

lay corporation, 28.

civil corporation, 26, 28.

public corporation, 26, 29.

private corporation, 26, 29.

stock corporation, 26, 31.

nonstock corporation, 26, 31.

quasi corporations, 26, 31.

foreign corporations, 74-80, 612.

corporations by prescription, 84, 86.

capital, 256.

capital stock, 256.

[The figures refer to pages.]

DEFINITION—Continued.

shares, 257.
certificates of stock, 260.
common stock, 362
preferred stock, 362.
guaranteed stock, 362.
dividend, 342.
stock dividend, 350.

DELEGATION,

of power to create corporation, 34, 40.
performance of ministerial acts, 34, 41.

DEPOSIT,

payment of, by subscriber, 312.

DEVISE,

to corporation, 129, 131.

DIRECTORS,

see "Officers and Agents."

DISCHARGE,

of subscriber, see "Subscriptions to Stock."

DISSOLUTION OF CORPORATION,

how effected, 231-248.
expiration of charter, 232.
by act of the legislature, 201, 218, 233.
loss of integral part, death or loss of members, 234.
surrender of charter, 235.
loss or surrender of property, 236.
abandonment of franchises or business, 236.
forfeiture of charter, 237.
 who may declare, 237, 242.
 necessity for judicial proceeding, 237, 238.
 when forfeiture will be decreed, 238, 239.
 waiver of forfeiture, 241.
 modes of proceeding to enforce, 244.
equity jurisdiction, 245.
effect of dissolution, 248.
 exercise of corporate powers, 249.
 actions and proceedings after dissolution, 249.
 judgment rendered after dissolution, 249.
 extinguishment of debts, 250.
 reversion and escheat of property, 250-252.
 equity jurisdiction over assets, 250.

[The figures refer to pages.]

DISSOLUTION OF CORPORATION—Continued,

effect as to creditors, 555.

acts of members as acts of corporation, for purpose of forfeiture, 9.

extension of charter, 81.

DISTRIBUTION,

of shares in case of excessive subscriptions, 308, 313.

DIVIDENDS,

rights as to profits and dividends, 340–358.

“dividend” defined, and distinguished from profits, 342.

no right to profits until dividend declared, 342.

right to dividend vests when it is declared, 342, 343.

when dividends may be declared, 344.

discretion of directors as to declaring, 347.

who entitled to dividends, 348.

effect of transfer of shares, 348, 349, 412.

how payable, 350.

stock dividends, 350.

set off against debt due to corporation, 351.

remedies of stockholders, 351.

interest, 352.

statute of limitations, 352.

remedies where dividends are improperly paid, 353.

on preferred stock, 365.

grants and bequests of income and profits of stock, 354–358.

rights as between life tenant and remainder-man, 354–358.

DOMICILE,

see “Citizenship”; “Foreign Corporations.”

DRUNKEN PERSONS,

as subscribers to stock, 275.

E

ECCLESIASTICAL CORPORATION,

defined, 28.

ELECTIONS,

see “Meeting of Stockholders”; “Officers and Agents.”

ELEEMOSYNARY CORPORATION,

defined, 28, 28.

EMINENT DOMAIN,

power of state, 211.

ENTITY,

corporate entity explained, 5 et seq.

[The figures refer to pages.]

EQUITY,

- suits by stockholders, interference in management, 389-401.
 - acts within power of majority, and discretionary powers, 396.
 - rule stated by the United States supreme court, 398.
 - laches and estoppel, 399.
 - motive of stockholder suing, 400.
 - parties to suit, 400.
 - to compel declaration of dividend, 347, 351.
- jurisdiction to dissolve corporation, 245.
- jurisdiction over assets of dissolved corporation, 250.
- suits by creditors, see "Creditors of Corporations."

ESCHEAT,

- of property on dissolution of corporation, 250-252.

ESROW,

- conditional delivery of subscription, 306.

ESTOPPEL,

- by contract or otherwise, to deny organization and existence of corporation, 62, 99-108.
 - necessity for recognition of corporate existence 102.
 - the doctrine based upon equitable grounds, 103.
 - unlawful assumption of corporate powers, 104.
 - the doctrine not limited to de facto corporations, 99.
- of subscriber to stock, to deny corporate existence, 100.
- to dispute validity of subscription, 335.

EVIDENCE,

- proof of corporate existence, 82-85.
- of acceptance of charter, presumption, 51, 53.
 - of amendment, 53.
- presumption of charter, corporations by prescription, 54, 56.
- presumptions of corporate power, 129, 135, 155.
- parol evidence of condition in subscription, 301.
- oral subscriptions to stock, 277, 278.

EXCLUSIVE PRIVILEGES,

- power to grant, 36.
- power of state, 205.

EXECUTION,

- property of corporation subject to, 533.
- levy upon shares of stock, 257, 258.

EXECUTOR OR ADMINISTRATOR,

- power of corporation to act as, 132.

[The figures refer to pages.]

EXEMPLARY DAMAGES,

see "Torts."

EXEMPTION,

from taxation, see "Taxation."

EXPIRATION OF CHARTER,

extension, 81.

effect, 89.

EXPULSION,

of members, 401-405.

by-laws, 456.

EXTENSION OF CHARTER,

in general, 81.

distinguished from creation of new corporation, 81.

effect, 81.

F**FEDERAL CORPORATIONS,**

power of congress to create, 34, 39.

in District of Columbia, 34, 40.

not controllable by the states, 40.

FOREIGN CORPORATIONS,

defined, 74-80, 612.

status, in general, 612.

power to act in another jurisdiction, 613.

comity, 613, 615.

right to exclude or impose conditions, 615.

taxation, 616.

requiring deposit, 617.

requiring appointment of agent, and submission to jurisdiction of courts, 617.

interstate commerce, 617, 618.

absolute exclusion, sufficiency of grounds, 618, 619.

foreign corporation in fraud of the laws of a state, or contrary to its policy, 620.

retaliatory statutes, 622.

what constitutes "doing business" in the state, 623.

effect of noncompliance with statute, contracts, etc., 626.

estoppel, 628.

powers of foreign corporation, limitation of its charter, 630.

limitation of the local law, 631.

foreign corporations de facto, 88, 632.

rights and immunities of members, 632.

[The figures refer to pages.]

FOREIGN CORPORATIONS—Continued.

- quo warranto and mandamus, 632.
- actions by, 633, 634.
- actions against, 633, 634.
 - service of process, 634, 635.
 - attachment of property, 636.
 - effect of judgment against, 636.
 - jurisdiction of federal courts, 637.
- visitorial power of state over foreign corporation, 639.
 - cannot enforce forfeiture of charter, 639.
 - other illustrations, 639, 640.
 - dissolution, 640.

FORFEITURE OF CHARTER,

- in general, 237-244.
- vacation by legislature, 238, 239.
- who may enforce, 237, 242.
- necessity for judicial proceedings, 237, 238.
- when forfeiture will be decreed, 238, 239.
- waiver of forfeiture, 241.
- modes of proceedings to enforce, 244.
- equity jurisdiction, 245.
- see "Dissolution."

FORFEITURE OF SHARES,

- for nonpayment of assessments, 318, 319.
- action and forfeiture as cumulative remedies, 318, 321.
- effect, 321, 334.
- by-laws, 456, 458.

FORGED TRANSFER,

- see "Transfer of Shares."

FORMATION,

- see "Creation of Corporations."

FRANCHISE,

- see "Creation of Corporations"; "Powers and Liabilities."

FRAUD,

- liability of corporation, 193, 195.
 - see "Officers and Agents"; "Torts."
- in procuring subscriptions to stock, 283.
 - authority of agents, 284.
 - what constitutes fraud, 285.
 - effect, ratification, and laches, 289.
- of promoters, 117.

[The figures refer to pages.]

FRAUD—Continued,

in organization of corporation, 96.

see "Watered and Bonus Stock."

FRAUDS, STATUTE OF,

whether applicable to contracts for sale of shares, 258, 259.

not applicable to subscriptions to stock, 277.

FRAUDULENT CONVEYANCES,

by corporations, 549.

G

GENERAL AND SPECIAL LAWS,

see "Creation of Corporations."

GRATUITOUS STOCK,

see "Watered and Bonus Stock."

GUARANTIED STOCK,

defined, 362.

see "Preferred Stock."

GUARANTY,

see "Contracts."

GUARDIAN,

power of corporation to act as, 132.

H

HUSBAND AND WIFE,

see "Married Women."

I

ILLEGAL CONTRACTS,

see "Contracts"; "Ultra Vires."

INCOME AND PROFITS OF SHARES,

see "Dividends."

INCORPORATION,

see "Creation of Corporations."

INCREASE,

of stock, see "Capital Stock."

INFANTS,

as subscribers to stock, 275.

INHABITANT,

corporation as a, 24.

[The figures refer to pages.]

INJUNCTION,

- see "Equity."
- suit by stockholders, see "Stockholders and Members."
- suit by creditors, 552.
- see "Creditors of Corporations."

INSANE PERSONS,

- as subscribers to stock, 275.

INSOLVENCY,

- does not dissolve, 236, 237.

INSPECTION OF BOOKS AND PAPERS,

- right of stockholders or members, 336-339.

INSURANCE COMPANIES,

- powers, generally, see "Powers and Liabilities."
- lending money on discount of notes, 138, note.
- borrowing money, 145.

INTEREST,

- on subscription to stock, 327.
- on dividends, 352.

INTERPRETATION,

- of charters, see "Charters."

IRREGULAR INCORPORATION,

- see "De Facto Corporations"; "Estoppel"; "Partnership."

J**JOINT-STOCK COMPANY,**

- in general, 21.

JOINT TENANCY,

- power to hold in joint tenancy, 181.

JUDGMENT,

- against foreign corporation, 636.
- against corporation after dissolution, 249.

JURISDICTION,

- see "Actions"; "Equity."

K**KNOWLEDGE,**

- notice to officer or agent as notice to corporation, 502.

[The figures refer to pages.]

L

LAY CORPORATIONS,

defined, 28.

LEASES,

by corporation, power, 134, 136, 138, 142.

railroad or other quasi public corporation, 134, 136, 138, 142.

LEGISLATIVE CONTROL,

see "State Control."

LEGISLATURE,

see "Congress"; "State Legislature"; "Territorial Corporations."

LIBEL,

liability of corporation for, 193, 195.

see "Torts."

LICENSE,

see "Foreign Corporations."

LIEN,

of corporation on shares, 413, 457.

LIMITATION OF ACTIONS,

to recover dividend, 352.

action by corporation against officers and agents, 520.

LOANS,

see "Contracts."

M

MAJORITY,

powers of the majority, in full, 443-453.

in general, 443, 445.

where the power of management is vested in the directors, 443, 447.

power to accept amendment of charter, 444, 447.

must act at a meeting duly held, 462, 464.

power to make by-laws, 454.

see "By-Laws."

increase of capital stock, 358.

MALICIOUS PROSECUTION,

liability of corporation, 193, 196.

see "Torts."

MANAGEMENT OF CORPORATIONS,

powers of the majority of stockholders, 443-453.

in general, 443, 445.

where the power of management is vested in the directors, 443, 447.

power to accept amendment or alteration of charter, 444, 447.

Clk.Pr.Corp.—45

[The figures refer to pages.]

MANAGEMENT OF CORPORATIONS—Continued,

- must act at a meeting duly held, 462, 464.
- power to accept amendment or alteration of charter, 444, 447.
- by-laws, 454-462.
 - by whom enacted, 454.
 - must be proved, not judicially noticed, 455.
 - validity, 455 et seq.
 - providing for election, appointment, and removal of officers and agents, 455.
 - limiting powers and prescribing duties of officers and agents, 455, 467.
 - provision for corporate meetings, 455.
 - regulating right to vote, 455.
 - regulating transfers of shares, 455, 457.
 - expulsion of members, 456.
 - restraint of trade, 456.
 - giving lien on shares, 457.
 - providing for forfeiture of shares, 456, 458.
 - must be reasonable, 455, 456.
 - must be general, 456.
 - must be consistent with charter, 458.
 - cannot deprive stockholder of vested rights, 459.
 - partial invalidity, 459.
 - effect as to stockholders, 460.
 - effect as to third persons, 460.
 - repeal and amendment, 461.
 - waiver of by-law, 462.
- stockholders' meetings, 462.
 - necessity, 464.
 - calling meetings, 464.
 - notice of meeting, 464.
 - time and place of meeting, 466.
 - conduct of meeting, 468.
 - quorum and majority, 469.
 - disability of individual stockholders, 470.
 - record and proof of action, 471.
 - cure of irregularity by ratification, 471.
 - presumption of regularity, 471.
 - adjourned meetings, 472.
 - equity jurisdiction, 472.
 - voting, 473-482.
 - who entitled to vote, in general, 474.
 - pledgor and pledgee, 475.
 - trustees, 475.

[The figures refer to pages.]

MANAGEMENT OF CORPORATIONS—Continued,

- shares held by the corporation, 475.
- shares owned jointly, 476.
- restrictions in charter or statute, 476.
- evasion of charter or statutory provision, 476.
- personal interest of stockholder, 477.
- number of votes, 477.
- cumulative voting, 478.
- votes by proxy, 479.
- effect of illegal reception or rejection of votes, 481.
- election and appointment of officers and agents, 482.
- qualifications of directors and other officers, 484.
- powers of directors, 485.
 - directors de facto, 487.
 - appointment of agents, and ratification, 487.
 - must act as a board, 488, 489.
 - directors' meetings and resolutions, 488.
 - special meetings, 490.
 - place of meeting, 490.
 - notice of meeting, 491.
 - quorum and majority, 492.
 - record of proceedings, 493.
- authority of other officers and agents, in general, 493.
 - president, 495.
 - treasurer, 496.
 - cashier of bank, 497.
 - effect of charter and by-laws, 497.
 - holding out, agency by estoppel, 498.
 - agency by ratification, 500.
 - negotiable instruments, 501.
 - ultra vires contracts by agents, 501.
- notice to officer or agent as notice to corporation, 502.
- contracts between stockholder and corporation, 504.
- relation between officers and corporation, 504.
 - a fiduciary relation, 504.
 - fraud and breach of trust, 504.
 - contracts and other transactions between officers and corporation, 508.
 - contract or transaction by officer with himself, 508.
 - personal interest of officer in contract or transaction, 509.
 - extent of personal interest, 510.
 - where corporation is represented by other agents, 511.
 - consent, acquiescence, and laches of corporation or stockholders, 513.
 - liability of corporation to extent of benefit, 514.

[The figures refer to pages.]

MANAGEMENT OF CORPORATIONS—Continued,

- liability of officers to corporation, 514.
 - mistakes or errors of judgment, 515.
 - breach of trust, 515.
 - violation of charter or by-laws, 515.
 - negligence, 516.
- remedies against officers, 519.
 - statute of limitations, 520.
- liability of officers and agents to third persons, on contracts, 521.
- liability of corporation for torts of officers and agents, 523.
 - ratification, 527.
 - ultra vires, 528.
- liability of officers and agents to third persons for torts, 530.
- compensation of officers, 531.
- removal of officers and agents, 533.
- relation between officers and stockholders, 534.
- interference and suits by individual stockholders, 389-401.
 - laches and estoppel, 399.
- interference by creditors, 546.

MANAGERS,

- see "Officers and Agents."

MANDAMUS,

- to compel court or officer to issue certificate of incorporation, etc., 41.
- to recover or compel declaration of dividend, 353.
- by stockholder, to enforce right to inspect books, 386.
- by foreign corporation, 632.

MANUFACTURING COMPANIES,

- powers of, see "Powers and Liabilities."

MARRIED WOMEN,

- as subscribers to stock, 275.

MEETING OF DIRECTORS,

- in general, 488.
- special meetings, 490.
- place of meeting, 490.
- notice of meeting, 491.
- quorum and majority, 492.
- record of proceedings, 493.

MEETINGS OF STOCKHOLDERS,

- in general, 462.
- necessity, 464.
- calling meetings, 464.

[The figures refer to pages.]

MEETINGS OF STOCKHOLDERS—Continued,

- notice of meeting, 464.
- time and place of meeting, 466.
- conduct of meeting, 468.
- quorum and majority, 469.
- disability of individual stockholders, 470.
- record and proof of action, 471.
- cure of irregularity by ratification, 471.
- presumption of regularity, 471.
- adjourned meetings, 472.
- equity jurisdiction, 472.
- by-laws regulating, 455.
- voting, 473-482.
 - who entitled to vote, in general, 474.
 - by-laws regulating, 455.
 - pledgor and pledgee, 475.
 - trustees, 475.
 - shares held by corporation, 475.
 - shares owned jointly, 476.
 - restrictions in charter or statute, 476.
 - evasion of charter or statute, 476.
 - personal interest of stockholder, 477.
 - number of votes, 477.
 - cumulative voting, 478.
 - voting by proxy, 479.
 - effect of illegal reception or rejection of votes, 481.

MEMBERS,

- see "Stockholders or Members."

MERGER,

- of members in corporation, 5 et seq.

MISNOMER,

- of corporation, effect, 74.

MISTAKE,

- subscriptions to stock, 290.

MONOPOLY,

- power to grant exclusive privileges, 36.

MORTGAGES,

- power of corporation to mortgage property, 134, 136, 138, 142.
- railroad or other quasi public corporation, 134, 136, 138, 143.
- power of corporation to take, 132.

MORTMAIN,

- statutes of, 129.

[The figures refer to pages.]

MUNICIPAL CORPORATIONS,

- as subscribers to stock, 276.
- distinguished from private corporations, 29.

N

NAME OF CORPORATION,

- in general, necessity, 17, 71, 122.
- choice of name, 71, 72.
- taking name of another corporation, 71, 72.
- acquisition by user or reputation, 73.
- change of name, 73.
 - special act authorizing change, 44.
 - effect, 73, 74.
- effect of misnomer, 74.

NEGLIGENCE,

- liability of corporation, 193, 195.
 - see "Torts."
- of officers and agents, see "Officers and Agents"; "Torts."

NEGOTIABLE INSTRUMENTS,

- see "Contracts."
- want of authority in officer or agent executing, 501.

NONRESIDENCE,

- of corporators, 66.
- nonresidents, as subscribers to stock, 275.

NONSTOCK CORPORATIONS,

- defined, 26, 31.

NOTES,

- see "Contracts."

NOTICE,

- to officer as notice to corporation, 502.

NUMBER,

- of corporators, 56, 64.

O

OBJECT OF INCORPORATION,

- see "Purpose of Incorporation."

OBLIGATION OF CONTRACTS,

- see "State Control."

OFFICERS AND AGENTS,

- election and appointment, 157, 482.
- by-laws, 455.

[The figures refer to pages.]

OFFICERS AND AGENTS—Continued,

- qualification of directors and other officers, 484.
- powers of directors, 485.
 - directors de facto, 487.
 - appointment of agents and ratification, 487.
 - must act as a board, 488, 489.
 - directors' meetings, 488.
 - special meetings, 490.
 - place of meeting, 490.
 - notice of meeting, 491.
 - quorum and majority, 492.
 - record of proceedings, 493.
- authority of other officers and agents, in general, 493.
 - president, 495.
 - treasurer, 496.
 - cashier of bank, 497.
 - effect of charter and by-laws, 455, 497.
 - holding out, agency by estoppel, 498.
 - agency by ratification, 500.
 - negotiable instruments, 501.
 - ultra vires contracts by agents, 501.
- notice to officer as notice to corporation, 502.
- contracts between stockholder and corporation, 504.
- relation between officers and corporation, 504 et seq.
 - a fiduciary one, 504.
 - fraud and breach of trust, secret profits and personal benefit, 504.
 - contracts and other transactions between officers and corporation, 508.
 - contract or transaction by officer with himself, 508.
 - personal interest in contract or transaction, 509.
 - extent of personal interest, 510.
 - where corporation is represented by other agents, 511.
 - consent, acquiescence, and laches of corporation or stockholders, 513.
 - liability of corporation to extent of benefit, 514.
- liability of officers to corporation, 514.
 - mistake or error of judgment, 515, 353.
 - breach of trust, 515.
 - violation of charter or by-laws, 515.
 - negligence, 516, 353.
- remedies against officers, 519.
 - statute of limitations, 520.
- discretion as to declaring dividends, 347.
- who authorized to increase capital stock, 358.
- liability of officers and agents to third persons on contracts, 521.

[The figures refer to pages.]

OFFICERS AND AGENTS—Continued,

- liability of corporation for torts of officers and agents, 284, 528.
- ratification, 527.
- ultra vires, 528.
- agents to receive subscriptions, 238.
- as subscribers to stock, 277.
- liability of officers and agents to third persons for torts, 530.
- compensation, 531.
- removal, 533.
- by-laws, 455.
- relation between officers and stockholders, 534.
- liability to creditors, 605-611.
- preferences to officers who are creditors, 608.
- statutory liability, 609.
- promoters, see "Promoters."

ORGANIZATION,

- see "Creation of Corporations."

P

PAROL EVIDENCE,

- see "Evidence."

PARTNERSHIP,

- distinguished from corporation, 12 et seq.
- liability of associates of pretended corporation as partners, 108.

PAYMENT,

- in whole or in part for stock, as condition precedent to incorporation, 58.
- of deposit by subscriber, 313.
- of subscriptions, in part only, 368 et seq.
- of subscriptions, in property, 369 et seq.
- of dividends, see "Dividends."
- see "Watered and Bonus Stock."

PERPETUAL SUCCESSION,

- the faculty of, 12, 15.

PERSON,

- corporation as a, 24.

PERSONAL PROPERTY,

- power to take and hold, 128.
- by gift or bequest, 129.
- power to sell, convey, mortgage, or pledge, 134, 136, 138, 142.
- power to purchase, 135-142.

[The figures refer to pages.]

PLACE,

of organisation, outside the state, 54.

PLEDGE,

power of corporation to pledge property, 134.

POLICE POWER,

of state over corporations, 207-211.

POWERS AND LIABILITIES OF CORPORATION,

in general, 120.

express powers, 122.

powers incidental to corporate existence, 122.

perpetual succession, 122.

corporate name, 122.

power to sue, in general, 122.

to contract, see "Contracts."

to use common seal, 123, 134, 136, 156.

to make by-laws, see "By-Laws."

motion or removal of members, see "Expulsion of Members."

powers implied from those expressly granted, 124, 138.

construction of charters, in general, 124.

in favor of the public in case of doubt, 125.

general terms following special terms, 125, 127.

express mention and implied exclusion, 125, 128, 129.

power to take and hold real and personal property, 128.

by gift or bequest, 129.

by devise, 129, 131.

enumeration of purposes as an exclusion of others, 129.

limitation as to amount or value of property, 129.

presumption of power, 129.

statutes of mortmain, 129.

power to take fee, 130.

reversion, 130.

joint tenancy, 130.

tenancy in common, 131.

conflict of laws, 131.

devise for use of corporation, 131.

power to take mortgage, 132.

power to act as trustee, executor, guardian, etc., 132.

power as to contracts and conveyances, see "Contracts"; "Conveyances";
"Leases"; "Mortgages"; "Pledge."

liability for torts, see "Torts."

liability for acts of officers or agents, see "Officers and Agents."

criminal responsibility, see "Crimes."

[The figures refer to pages.]

POWERS AND LIABILITIES OF CORPORATION—Continued,

power to increase capital stock, 358.

issuing preferred stock, 361-368.

see "Preferred Stock."

issue of watered or bonus stock, 368-383.

see "Watered and Bonus Stock."

POWERS OF MAJORITY,

see "Majority."

PREFERRED STOCK,

in full, 361-368.

defined, 361, 362.

power to create, 361, 362.

amendment of charter authorizing, 364.

liabilities and estoppel of stockholders to object, 364.

rights and liabilities of holders, 365.

dividends, 365.

liability to creditors, 367.

status as creditors, and not as stockholders, 365, 367.

PREFERRING CREDITORS,

validity of preferences, 553.

PRESCRIPTION,

corporations by, 34, 36.

PRESIDENT,

see "Officers and Agents."

PRESUMPTION,

of charter, corporations by prescription, 34, 36.

of acceptance of charter, 51, 53.

of corporate power, 129, 135, 155.

PRINCIPAL AND AGENT,

see "Agency"; "Officers and Agents."

PRINCIPAL AND SURETY,

see "Contracts."

PRIVATE CORPORATIONS,

distinguished from public, 26, 29.

PROFITS,

see "Dividends."

PROMOTERS,

relation between corporation and its promoters, 111-119.

liability of corporation for expenses and services of promoters, 111.

liability on contracts by promoters, 112.

liability of promoters, secret profits, etc., 117.

[The figures refer to pages.]

PROOF,

see "Evidence."

PROPERTY OF CORPORATION,

is not owned by the members individually, 5 et seq.

members cannot convey individually, 6, 7.

nor sue at law for injury to, 7.

otherwise under some circumstances in equity, 11.

not attachable for debts of members, 7.

insurable interest of members, 6, note.

PROXY,

voting by proxy at stockholders' meeting, 479.

PUBLIC CORPORATIONS,

defined, and distinguished from private, 26, 29.

PURPOSE OF INCORPORATION,

for what purposes corporation may be formed, 67.

construction of general clause of enabling act, 69.

restrictions of federal constitution on power of states, 37, 38.

power of congress, 34, 39.

grant of exclusive privileges, 38.

Q**QUASI CORPORATIONS,**

defined, 27, 31.

QUORUM,

see "Meetings of Directors"; "Meetings of Stockholders."

QUO WARRANTO,

against foreign corporation, 632.

see "State Control."

R**RAILROAD COMPANIES,**

powers, to take and hold land, 129.

to aid in maintenance of steamboat line by another, 136.

to purchase and operate a steamboat, 136.

lease and operation of another road, 136.

lease or transfer of its own road, 136.

consolidation agreement, 136.

lease of telegraph line to another, 136.

contract to carry over connecting line, 139.

restriction as to motive power, 140.

purchase of real or personal property, 140, 141.

dealing in bills and notes, 141.

[The figures refer to pages.]

POWERS AND LIABILITIES OF CORPORATION—Continued,

- power to increase capital stock, 358.
- issuing preferred stock, 361-368.
 - see "Preferred Stock."
- issue of watered or bonus stock, 368-369.
 - see "Watered and Bonus Stock."

POWERS OF MAJORITY,

- see "Majority."

PREFERRED STOCK,

- in full, 361-368.
- defined, 361, 362.
- power to create, 361, 362.
- amendment of charter authorizing, 364.
- liaches and estoppel of stockholders to object, 364.
- rights and liabilities of holders, 365.
 - dividends, 365.
 - liability to creditors, 367.
 - status as creditors, and not as stockholders, 365, 367.

PREFERRING CREDITORS,

- validity of preferences, 553.

PRESCRIPTION,

- corporations by, 34, 36.

PRESIDENT,

- see "Officers and Agents."

PRESUMPTION,

- of charter, corporations by prescription, 34, 36.
- of acceptance of charter, 51, 53.
- of corporate power, 129, 135, 155.

PRINCIPAL AND AGENT,

- see "Agency"; "Officers and Agents."

PRINCIPAL AND SURETY,

- see "Contracts."

PRIVATE CORPORATIONS,

- distinguished from public, 26, 29.

PROFITS,

- see "Dividends."

PROMOTERS,

- relation between corporation and its promoters, 111-119.
- liability of corporation for expenses and services of promoters.
- liability on contracts by promoters, 119.
- liability of promoters, secret.

PR: P

see "Firm"

PR: P

in the case of a firm, the firm is not a partner in the business.

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PUBLIC: P

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PURPOSE: P

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Q

QUANT: P

in the case of a firm, the firm is not a partner in the business.

QUORUM: P

see "Meetings of Directors"; "Meetings of Stockholders."

QUO WARRANT: P

in the case of a firm, the firm is not a partner in the business.

see "Bank Charter."

R

RAILROAD COMPANIES: P

power to take and hold land, 129.

to aid in maintenance of steamboat line by another, 136.

to purchase and operate a steamboat, 136.

line and operation of another road, 136.

line or transfer of its own road, 136.

consolidation agreement, 136.

line of telegraph line to another, 136.

contract to carry over connecting line, 136.

subscription as to motive power, 140.

purchase of real or personal property, 140, 141.

issuing in bills and notes, 141.

[The figures refer to pages.]

RAILROAD COMPANIES—Continued,

sale, lease, mortgage, or pledge of property, 142, 143.
contracts of guaranty or suretyship, 143.

RATIFICATION,

of claim to corporate existence, 48.
by corporation of contracts of officer or agent, 500.
of torts, 527.

REAL PROPERTY,

power to take and hold, 123:
by devise, 129, 131.
enumeration of purposes as an exclusion of others, 129.
limitation as to amount or value, 129.
presumption of power, 129.
statutes of mortmain, 129.
power to take in fee, 130.
reversion, 130.
joint tenancy, 130.
tenancy in common, 131.
conflict of laws, 131.
devise for use of corporation, 131.
power to take mortgage, 132.
power to sell and convey or mortgage, 134, 136, 138, 142.
power to purchase, 135-142.

RECEIVERS,

suits by creditors, 552.
suits by stockholders, 389.
suits by creditors for appointment, 58.

REGISTRATION,

of transfer, see "Transfer of Shares."

RELEASE,

of subscriber, see "Subscriptions to Stock."

RELIGIOUS CORPORATIONS,

defined, 26, 28.
powers, generally, see "Powers and Liabilities."
contracts in raising money for church purposes, 133.

REMEDIES,

see "Actions"; "Equity"; "Injunction"; "Mandamus"; "Quo Warranto."

REMOVAL,

of members, 401-405.
of officers, 533.
by-laws, 455.

[The figures refer to pages.]

REPUTATION,

acquisition of corporate name by, 73.

RESIDENCE,

of corporation, 74-80.

for purpose of jurisdiction of federal courts. 75-80.

where there are charters from several states. 75, 77.

charter distinguished from license, 75, 80.

of corporators, 66.

REVERSION,

of property on dissolution of corporation, 130, 250-252.

REVOCATION,

of subscription to stock, 267, 271.

S**SALES,**

power of corporation to purchase property, 128, 135-142.

power to sell, 134, 136, 138, 142.

railroad and other quasi public corporations, 134, 136, 138, 143.

sale of franchise, 134, 143.

of shares, see "Transfer of Shares."

distinguished from subscription, 262.

statute of frauds, 258, 259.

see "Contracts."

SEAL,

corporate seal, 19.

see "Contracts."

SET-OFF AND COUNTERCLAIM,

against dividend, 351.

by debtor of corporation, 557.

by stockholder as against creditors, 602.

SHARES,

defined, 257, 258.

not a chattel interest, but in the nature of chose in action, 258.

not real estate, 258.

execution and attachment of shares, 259.

transferrability, 18.

transfer of, see "Transfer of Shares."

forfeiture, see "Forfeiture of Shares."

SLANDER,

liability of corporation, 193.

see "Torts."

[The figures refer to pages.]

SOLE CORPORATION,

in general, 26, 27.

SPECIAL LAWS,

see "Creation of Corporations."

STATE CONTROL,

power of the state over corporations, 201-230.

the charter as a contract not to be impaired, 201, 202

contract between corporation and members, 204.

creating similar corporation, 204, 205.

where exclusive privilege has been granted, 205.

contracts between corporation and third persons, 206.

change of remedies, 206.

police power of state, 207-211.

power of eminent domain, 211.

reservation of power to alter or repeal charter, 212-219.

in constitution or general law, 213.

acceptance of amendment, 213.

changes authorized by reservation, 214-219.

vacation of charter for misuser, 218.

offer of amendment, power of majority, 219.

taxation of corporations, 219-230.

the power in general, 221.

object of taxation, 221.

jurisdiction, 222.

property taxable, 222.

double taxation, 223.

place of taxation, 224.

restrictions in federal constitution, 224.

equality and uniformity, 224.

United States bonds, 225.

regulation of commerce, 225.

federal corporations, 226.

exemption from taxation, 227.

doctrine of ultra vires, 230.

foreign corporations, 230.

forfeiture and dissolution, 231.

STATE LEGISLATURE,

power to incorporate, 34.

grant of exclusive privileges, 36.

enactment of laws, two-thirds vote, 37.

restriction as to subject and title of laws, 37.

restrictions in federal constitution, 37, 38.

[The figures refer to pages.]

STATE LEGISLATURE—Continued,

- delegation of power to create corporation, 34, 40.
- performance of ministerial acts, 34, 41.
- ratification of claim to corporate existence, 44.
- power over corporations, see "State Control."

STATUTES,

- of mortmain, 129.
- of wills, 131.
- of frauds, whether applicable to contracts for sale of shares, 258, 259.
- not applicable to subscriptions to stock, 277.
- general and special laws, see "Creation of Corporations."

STOCK,

- see "Capital Stock."

STOCK CORPORATIONS,

- defined and distinguished from nonstock, 26, 31.

STOCK DIVIDENDS,

- defined, right to declare, 350.

STOCKHOLDERS' MEETINGS,

- see "Meeting of Stockholders."

STOCKHOLDERS OR MEMBERS,

- distinct from the corporation, 5.
- merger in corporate entity, 5.
- do not own the corporate property, 6, 7.
- cannot convey corporate property, 6, 7.
- cannot sue at law for injury to corporate property, 7.
 - otherwise, under some circumstances in equity, 11.
- cannot bind corporation by contracts, 7.
- their declarations or admissions not binding on corporation, 7.
- insurable interest in corporate property, 6, note.
- may contract with corporation, or convey to or take from it, 8.
- may sue corporation, and be sued by it, 8.
- action by or against corporation, not by or against members, 8.
- demands of, as set-off to demand against corporation, 9.
- when acts of, considered acts of corporation, 9.
- change or death of, does not affect corporate existence or identity, 15.
- how membership is acquired, in general, 253.
 - nonstock corporations, 253, 254.
 - stock corporations, 253, 255.
- subscriptions to stock, 261 et seq.
 - after incorporation, 261.
 - distinguished from a sale of shares, 262.

[The figures refer to pages.]

STOCKHOLDERS OR MEMBERS—Continued,

- prior to incorporation, 263-274.
 - common-law subscriptions, 264.
 - nature as a contract, 264, 265.
 - formation of the contract, 264.
 - consideration, 267.
 - revocation or lapse, 268.
 - subscription under statutes, 271.
 - consideration and revocation, 271.
- agreements to pay subscription to trustees for corporation when formed, 272.
- distinction between present subscription and agreement to subscribe, 273.
- who may become subscribers, 275.
 - aliens and nonresidents, 275.
 - infants, 275.
 - insane and drunken persons, 275.
 - married women, 275.
 - corporations, 276.
 - municipal corporations, 276.
 - directors or officers, 277.
- form of subscription, 277-281.
 - at common law, 277.
 - necessity for writing, 277.
 - formalities required by statute, 278.
 - directory provisions, 280.
 - substantial compliance with statute, 280.
- mutual consent, 281.
- subscriptions induced by fraud, 283.
 - authority of agents, 284.
 - what constitutes fraud, 285.
 - effect of fraud, ratification and laches, 286.
- subscriptions under mistake, 290.
- subscription by agent, 291.
 - effect of want of authority, 292.
- agents to receive subscriptions, 293.
- conditional subscriptions, 294-302.
 - after organization of corporation, 296.
 - prior to incorporation, 299.
 - conditions must be expressed in the writing, 301.
 - waiver of conditions, 301.
- subscriptions upon special terms, 302.
 - distinguished from conditional subscriptions, 295, 302.
 - validity, 304.
 - who may receive, 306.

[The figures refer to pages.]

STOCKHOLDERS OR MEMBERS—Continued,

- conditional delivery of subscription, escrow, 306.
- subscription of entire capital, 297, 308.
- excessive subscription and distribution, 308, 313.
- payment of deposit, 313.
- delivery of certificate not essential to liability or rights, 316.
- remedy of corporation on subscriptions, 318-321.
 - action to recover assessments, 318.
 - forfeiture of shares, 318, 319.
 - action and forfeiture as cumulative remedies, 318, 321.
- calls and assessments, 322-327.
 - necessity, 323.
 - validity, 325.
 - notice and demand, 327.
 - interest, 327.
- assignment of unpaid subscription, 328.
- release and discharge of subscriber, 328-334.
 - withdrawal and release, 329.
 - reduction of shares, 329.
 - violation of charter by corporation, mismanagement, 331.
 - alteration or amendment of charter, 331.
 - loss or abandonment of business, property, or franchises, 333.
 - forfeiture of shares, 334.
 - transfer of shares, 334.
- estoppel of subscriber, 100, 335.
- increase of stock, 358.
 - shareholders' right to preference, 360.
- right to inspect books and papers of corporation, 336-339.
- rights as to profits and dividends, 340-358.
 - "dividend" defined, 342.
 - distinguished from "profits," 342.
 - no right to profits until dividend declared, 342.
 - right to dividend vests when it is declared, 342, 343.
 - when dividend may be declared, 344.
 - discretion of directors as to declaring, 347.
 - who entitled to dividends, 348.
 - effect of transfer of shares, 348, 349.
 - how payable, 350.
 - stock dividends, 350.
 - set-off against debt due to corporation, 351.
 - remedies of stockholders, 351.
 - interest, 352.
 - statute of limitations, 352.

[The figures refer to pages.]

STOCKHOLDERS OR MEMBERS—Continued,

- remedies where dividends are improperly paid, 353.
- grants and bequests of income and profits of stock, 354-358.
- rights as between life tenant and remainder-man, 354-358.
- preferred stock, 361-368.
 - defined, 361, 362.
 - power to create, 361, 362.
 - amendment of charter authorizing, 364.
 - laches and estoppel of stockholders to object, 364.
 - rights and liabilities of holders of, 365.
 - dividends, 365.
 - liability to creditors, 367.
 - status as creditors, and not stockholders, 365, 367.
- watered and bonus stock, 368-389.
 - defined, 368.
 - effect as to corporation, 368, 369.
 - effect as to stockholders, 368, 371.
 - effect as to creditors, 368, 372.
 - payment of original subscriptions, 368, 372.
 - increase of capital stock, 368, 374.
 - issue of stock at market value by active corporation to pay debts, etc., 368, 375.
 - gratuitous issue of stock, 369, 378.
 - payment for stock in property or services, 369, 379.
 - value of property or services, 369, 379.
 - creditors who cannot complain, 369, 383.
 - effect of constitutional and statutory provisions, 369, 384.
 - liability of transferees, 388.
- actions by, for injuries to corporations, and interference in management, 389-401.
 - at law, 389, 391.
 - in equity, 389, 392.
 - acts within power of majority, and discretionary powers, 395.
 - the rule as stated by the United States supreme court, 398.
 - laches and estoppel, 399.
 - motive of stockholder suing, 400.
 - parties to suits, 400.
- transfers of shares, 18, 406-442.
 - right to transfer, 406.
 - by-laws, 407.
 - agreement not to transfer, 409.
 - effect of transfer, 409-413.
 - liability for calls, 410.

[The figures refer to pages.]

STOCKHOLDERS OR MEMBERS—Continued,

- right to dividends, 412.
- statutory liability to creditors, 412.
- pledgees, trustees, etc., 413.
- lien of corporation on shares, 413.
 - by-laws, 414.
 - waiver, 414.
- validity of transfers, 415.
 - transfer after dissolution, 416.
 - mode of transfer, 416.
 - what law governs, 417.
- registration of transfer, 417.
 - the rules stated, 417-419.
 - necessity, as against corporation, 420.
 - as against estoppel of owner in case of unauthorized transfer, 422.
 - as against prior equities of third persons, 422.
 - as against creditors of the corporation, 422.
 - as against bona fide purchasers or pledgees, 423.
 - as against creditors of registered owner, 423.
 - failure to register as evidence of secret trust, 425.
- issue of new certificate, 427.
- forged and unauthorized transfers, 427.
 - transfers by trustees, 429.
 - estoppel of owner in case of unauthorized transfer, 431.
 - effect of judicial proceedings, 433.
- liability of indorser of forged certificate, 434.
- liability of corporation arising from unauthorized or invalid transfer, 435.
- liability of corporation on certificates issued fraudulently, without authority, etc., 437.
- remedy against corporation for refusal to recognize transfer, 440.
- compelling corporation to issue new certificates, 441.
- acceptance of amendment of charter, 53, 54.
- powers of the majority, see "Majority."
- relation between officers and stockholders or members, 534.
- expulsion of members, 401-405.
- liability to creditors, see "Creditors of Corporations."
- see "Corporators."

SUBSCRIPTIONS TO STOCK,

- after incorporation, 261.
 - distinguished from a sale of shares, 262.
- prior to incorporation, 263-274.
 - common-law subscriptions, 264.
 - nature as a contract, 264, 265.

[The figures refer to pages.]

SUBSCRIPTIONS TO STOCK—Continued,

- formation of the contract, 284.
- consideration, 287.
- revocation or lapse, 288.
- subscriptions under statutes, 271.
 - consideration and revocation, 271.
- agreements to pay subscriptions to trustees for corporation when formed, 272.
- distinction between present subscription and agreement to subscribe, 273.
- who may become subscribers, 275.
 - aliens and nonresidents, 275.
 - infants, 275.
 - insane and drunken persons, 275.
 - married women, 275.
 - corporations, 134, 151, 276.
 - municipal corporations, 276.
 - directors or officers, 277.
- form of subscription, 277-281.
 - at common law, 277.
 - necessity for writing, 277.
 - formalities required by statute, 278.
 - directory provisions, 280.
 - substantial compliance with statute, 280.
- mutual consent, 281.
- subscriptions induced by fraud, 283.
 - authority of agents, 284.
 - what constitutes fraud, 285.
 - effect of fraud, ratification and laches, 289.
- subscriptions under mistake, 290.
- subscription by agent, 291.
 - effect of want of authority, 292.
- agents to receive subscriptions, 293.
- conditional subscriptions, 294-302.
 - after incorporation, 296.
 - prior to incorporation, 299.
 - conditions must be expressed in the writing, 301.
 - waiver of conditions, 301.
- subscriptions upon special terms, 302.
 - distinguished from conditional subscriptions, 295, 302.
 - validity, 304.
 - who may receive, 306.
- conditional delivery of subscription, escrow, 306.
- subscription of entire capital, 297, 308.
- excessive subscription and distribution, 308, 313.

[The figures refer to pages.]

SUBSCRIPTIONS TO STOCK—Continued,

- payment of deposit, 313.
- delivery of certificate, 316.
- remedy of corporation on subscriptions, 318-321.
 - action to recover assessments, 318.
 - forfeiture of shares, 318, 319.
 - action and forfeiture as cumulative remedies, 318, 321.
- calls and assessments, 322-327.
 - necessity, 323.
 - validity, 325.
 - notice and demand, 327.
 - interest, 327.
- assignment of unpaid subscription, 328.
- release and discharge of subscriber, 328-334.
 - withdrawal and release, 329.
 - reduction of shares, 329.
 - violation of charter by corporation, mismanagement, 331.
 - alteration or amendment of charter, 331.
 - loss or abandonment of business, property, or franchises, 333.
 - forfeiture of shares, 321, 334.
 - transfer of shares, 334.
- estoppel of subscriber, 100, 335.
- subscriptions as a condition precedent to incorporation, 58.
- payment in whole or in part as a condition precedent, 58.
- increase of stock, 358.
 - shareholders' right to preference, 360.

SUBJECT OF ACTS,

- constitutional limitation, 57.

SUCCESSION,

- the faculty of, 12, 15, 122.

SUITS,

- see "Actions"; "Equity."

SURETYSHIP,

- see "Contracts."

T

TAXATION,

- of domestic corporation, see "State Control."
- of foreign corporation, see "Foreign Corporations."

TENANCY IN COMMON,

- power to hold as tenant in common, 131.

[The figures refer to pages.]

TERRITORIAL CORPORATIONS,

- power of territorial legislatures to create, 34, 40.
- effect of admission to statehood, 40.

TITLE OF ACTS,

- constitutional limitation, 37.

TORTS,

- responsibility of corporation for torts, 193.
- liability of corporation for torts of officers and agents, 523.
 - ratification, 527.
 - ultra vires, 528.
- fraud in procuring subscriptions, 284.
- liability arising from unauthorized or invalid transfer of shares, 435.
- liability on certificates of stock issued fraudulently, without authority, etc., 437.
- liability of officers and agents to third persons, 530.

TRANSFER OF SHARES,

- in full, 18, 406-442.
- right to transfer, 18, 406.
- by-laws, 407, 455, 457.
- agreement not to transfer, 409.
- effect of transfer, 409-413.
 - liability for calls, 410.
 - right to dividends, 348, 349, 354, 412.
 - statutory liability to creditors, 412.
 - pledgees, trustees, etc., 413.
- lien of corporation on shares, 413.
 - by-laws, 414, 457.
 - walver, 414.
- validity of transfers, 415.
- transfer after dissolution, 416.
- mode of transfer, 416.
- what law governs, 417.
- registration of transfer, 417.
 - the rules stated, 417-419.
 - as against corporation, 420.
 - as against estoppel of owner in case of unauthorized transfer, 422.
 - as against prior equities of third persons, 422.
 - as against creditors of the corporation, 422.
 - as against bona fide purchasers and pledgees, 423.
 - as against creditors of registered owner, 423.
 - failure to register as evidence of secret trust, 425.
 - issue of new certificate, 427.

[The figures refer to pages.]

TRANSFER OF SHARES—Continued,

forged and unauthorized transfers, 427 et seq.

transfers by trustees, 429.

estoppel of true owner, 431.

effect of judicial proceedings, 433.

liability of indorser of forged certificate, 434.

liability of corporation arising from unauthorized or invalid transfer, 435.

liability of corporation on certificates issued fraudulently, without authority.
etc., 437.

remedy against corporation for refusal to recognize transfer, 440.

compelling corporation to issue new certificate, 441.

liability of transferees of watered or bonus stock, 388.

TREASURER,

see "Officers and Agents."

TRESPASS,

liability of corporation, 198.

see "Torts."

TRUST COMPANIES,

power to act as trustee, 132.

TRUST-FUND DOCTRINE,

in general, 539-546.

TRUSTS,

power of corporation to act as trustee, 132.

devise in trust for use of corporation, 131.

relation between corporation and its promoters, 111, 117

see "Officers and Agents."

TURNPIKE COMPANIES,

power to engage as carriers, 136.

U

ULTRA VIRES,

effect of ultra vires act, in general, 163.

objection by state, forfeiture of charter, 163, 164.

injunction at suit of stockholder, 163, 164.

a corporation may exceed its powers, 164.

assent of shareholders, 166.

conveyances of land, or transfers of personalty, 167.

contracts, 170.

the doctrine that an ultra vires contract is illegal and void, 171.

ignorance of ultra vires character of transaction, 173.

unauthorized exercise of authorized powers, 174.

[The figures refer to pages.]

ULTRA VIRES—Continued,

- severable transaction, 175.
- negotiable bills and notes, 175.
- bonds, 175.
- actions quasi ex contractu, 177.
- suit in equity for accounting, 177.
- relief in equity against ultra vires contract, 178.
- borrowing money, subrogation of lender, 178.
- the doctrine allowing recovery on ultra vires contract, 179.
- action maintainable by corporation, 183.
- the ground of this doctrine, 183.
- necessity for performance by the plaintiff, 184.
- answers to arguments against this doctrine, 185.
- specific performance, 187.
- Illegal contracts in the strict sense, 187.
 - contracts disabling quasi-public corporation from performing duties, 188.
 - express prohibition in charter, 189.
 - effect of illegality, 190.
- liability for torts, see "Torts."
- responsibility for crime, see "Crimes."
- as a defense against taxation, 230.
- ultra vires acts as releasing subscription to stock, 331.

UNITED STATES,

- see "Congress."

USER,

- acquisition of corporate name by user or reputation, 78.

V

VISITORIAL POWER,

- see "State Control."

VOTING,

- see "Meetings of Stockholders."

W

WATERED AND BONUS STOCK,

- in full, 368-389.
- defined, 368.
- effect as to corporation, 368, 369.
- effect as to stockholders, 368, 371.
- effect as to creditors, 368, 372.
- payment of original subscriptions, 368, 372.

[The figures refer to pages.]

WATERED AND BONUS STOCK—Continued.

increase of capital stock, 368, 374.

issue of stock at market value by active corporation to pay debts, etc.,
368, 375.

gratuitous issue of stock, 369, 378.

payment for stock in property or services, 369, 379.

value of property or services, 369, 379.

creditors who cannot complain, 369, 383.

effect of constitutional and statutory provisions, 369, 384.

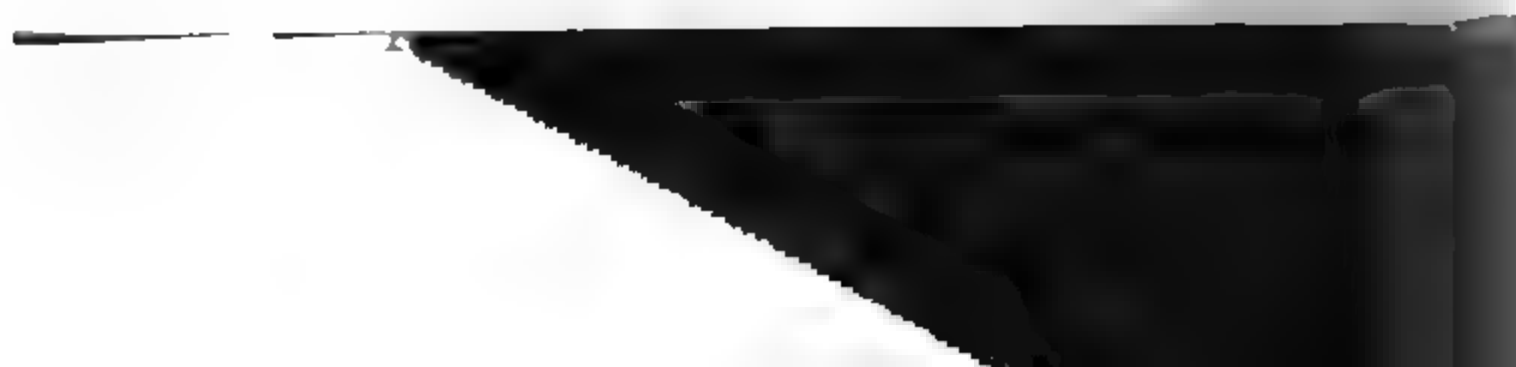
liability of transfers, 388.

WILLS,

power of corporation to take by devise or bequest, 129, 131.

conflict of laws, 131.

bequest of income and profits, dividends, 354-358.



1
2
3
4
5
6
7
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9
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11
12
13
14
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TABLE OF CONTENTS.

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TABLE OF CONTENTS.

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Chapter I.

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Chapter II.

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Chapter VI.

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Chapter VII.

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Chapter VIII.

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Chapter IX.

DUTIES AND LIABILITIES OF PARENTS: Maintenance, protection, and education of child; allowance out of child's estate; child as parent's agent; parent's liability for crimes and torts of child, etc.

Chapter X.

RIGHTS OF PARENTS AND OF CHILDREN: Right to custody; service and earnings of child; correction of child; emancipation of children; action by parent for injuries to child; gifts, contracts, and conveyances between; advancements; duty to support parent; domicile of child, etc.

PART III.

GUARDIAN AND WARD.

Chapter XI.

GUARDIANS DEFINED — SELECTION AND APPOINTMENT: Covering natural guardians; testamentary guardians; statutory guardians; guardians by estoppel; guardians of insane persons; guardians ad litem, etc.

Chapter XII.

RIGHTS, DUTIES, AND LIABILITIES OF GUARDIANS: Right to custody and services of ward; maintenance of ward; change of ward's domicile; management of ward's estate; foreign guardians; inventory and accounts; compensation of guardian; transactions between guardian and ward, etc.

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Chapter XIV.

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TABLE OF CONTENTS.

INTRODUCTION.

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Chapter I.

PERSONS IN INTERNATIONAL LAW: Covering states, their loss of identity, various unions of states, de facto states, belligerency and recognition thereof, and equality of states.

Chapter II.

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Chapter VI.

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Chapter VII.

INTERVENTION: Covering the subject generally.

Chapter VIII.

NATIONALITY: Covering citizenship, allegiance, expatriation, naturalization, etc.

Chapter IX.

TREATIES: Covering the subject generally.

Chapter X.

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Chapter XI.

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Chapter XII.

EFFECTS OF WAR—AS TO PERSONS: Covering the relations of enemies, noncombatants, privateers, prisoners of war, and the subjects of ransom, parole, etc.

Chapter XIII.

EFFECTS OF WAR—AS TO PROPERTY: Covering contributions, requisitions, foraging, booty, ransom, and other questions in regard to property.

Chapter XIV.

POSTLIMINIUM: The right and its limitations defined and explained.

Chapter XV.

MILITARY OCCUPATION: Covering the definition, extent, and effect of occupation, and the duties of an occupant.

Chapter XVI.

MEANS OF CARRYING ON HOSTILITIES: Covering the instruments and means of war, spies, etc.

Chapter XVII.

ENEMY CHARACTER: Covering enemies generally, domicile, houses of trade, property and transfer thereof, etc.

Chapter XVIII.

NON-HOSTILE RELATIONS: Covering commercia belli, flags of truce, passports, safe-conducts, truces or armistices, cartels, etc.

Chapter XIX.

TERMINATION OF WAR: Covering the methods of termination, uti possidetis, treaties of peace, conquest, etc.

Chapter XX.

OF NEUTRALITY IN GENERAL: Neutrality defined and explained.

Chapter XXI.

THE LAW OF NEUTRALITY BETWEEN BELLIGERENT AND NEUTRAL STATES: Covering the rights, duties, and liabilities of neutral states.

Chapter XXII.

CONTRABAND: Covering the subject generally.

Chapter XXIII.

BLOCKADE: Covering the subject generally.

Chapter XXIV.

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POWERS AND LIABILITIES OF CORPORATIONS (Continued): The doctrine of ultra vires.

Chapter VII.

POWERS AND LIABILITIES OF CORPORATIONS (Continued): Responsibility for torts and crimes; contempt of court.

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MEMBERSHIP IN CORPORATIONS (Continued): Covering transfer of shares.

Chapter XIII.

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TABLE OF CONTENTS.

INTRODUCTION.

Covering the definition, source, and nature of International Law.

Chapter I.

PERSONS IN INTERNATIONAL LAW: Covering states, their loss of identity, various unions of states, de facto states, belligerency and recognition thereof, and equality of states.

Chapter II.

THE COMMENCEMENT OF STATES—FUNDAMENTAL RIGHTS AND DUTIES: Covering the commencement and recognition of new states, effect of change of sovereignty, the fundamental rights and duties of states, etc.

Chapter III.

TERRITORIAL PROPERTY OF A STATE: Covering modes of acquiring property, boundaries, territorial waters, etc.

Chapter IV.

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Chapter V.

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Chapter VI.

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Chapter VII.

INTERVENTION: Covering the subject generally.

Chapter VIII.

NATIONALITY: Covering citizenship, allegiance, expatriation, naturalization, etc.

Chapter IX.

TREATIES: Covering the subject generally.

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Chapter XI.

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Chapter XII.

EFFECTS OF WAR—AS TO PERSONS: Covering the relations of enemies, noncombatants, privateers, prisoners of war, and the subjects of ransom, parole, etc.

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Chapter XIV.

POSTLIMINIUM: The right and its limitations defined and explained.

Chapter XV.

MILITARY OCCUPATION: Covering the definition, extent, and effect of occupation, and the duties of an occupant.

Chapter XVI.

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Chapter XVII.

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Chapter XVIII.

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Chapter XIX.

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Chapter XX.

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Chapter XXI.

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Chapter XXII.

CONTRABAND: Covering the subject generally.

Chapter XXIII.

BLOCKADE: Covering the subject generally.

Chapter XXIV.

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Chapter IV. LIABILITY OF MASTER TO THIRD PERSONS: Relationship; independent contractor; willful torts of servants, and independent torts.	Chapter X. DEATH BY WRONGFUL ACT: Right of action; instantaneous death, proximate cause of death, beneficiaries; damages; pleading and evidence; limitation of commencement of action.
Chapter V. COMMON CARRIERS OF PASSENGERS: The relation of passenger and carrier; termination of relation; who are passengers; the contract, ticket, compensation, etc.	Chapter XI. NEGLIGENCE OF MUNICIPAL CORPORATIONS: Public and private corporations; right of action; liability for injuries; alteration of grades; acts of officers or agents; acts ultra vires; judicial or legislative duties; conflagrations and destruction by mobs; public health and sanitation; quasi municipal corporations.
Chapter VI. CARRIERS OF GOODS: Definition; liability for loss or damage; liability for delay; contracts limiting liability in special states; limiting time and manner of making claims; construction of limiting contracts; actual notice; special classes of goods, as live stock and baggage; beginning and termination of liability; excuses for nondelivery.	

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TABLE OF CONTENTS.

ORIGIN AND HISTORY: Showing distinction between law and equity, equity jurisdiction in the United States, etc.	FRAUD as a ground of equitable relief; actual and constructive fraud, etc.
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- IX. Same (continued).
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- XII. Liability of Third Person to Principal.

Part III. RIGHTS AND LIABILITIES BETWEEN AGENT AND THIRD PER- SON.

- XIII. Liability of Agent to Third Person (including parties to contracts).
- XIV. Liability of Third Person to Agent.

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